SIMPLIFYING THE HOME BUYING PROCESS: HUD'S PROPOSAL TO REFORM RESPA

HEARING

BEFORE THE

SUBCOMMITTEE ON
HOUSING AND COMMUNITY OPPORTUNITY

OF THE

COMMITTEE ON FINANCIAL SERVICES
U.S. HOUSE OF REPRESENTATIVES

ONE HUNDRED EIGHTH CONGRESS

FIRST SESSION

FEBRUARY 25, 2003

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SIMPLIFYING THE HOME BUYING PROCESS: HUD'S PROPOSAL TO REFORM RESPA

Tuesday, February 25, 2003

U.S. House of Representatives,
Subcommittee on Housing and
Community Opportunity,
Committee on Financial Services,
Washington, D.C.

The subcommittee met, pursuant to call, at 2:07 p.m., in Room 2128, Rayburn House Office Building, Hon. Bob Ney [chairman of the subcommittee] presiding.

Present: Representatives Ney, Green, Bereuter, Baker, Shays, Hart, Tiberi, Harris, Waters, Lee, Watt, Miller of North Carolina, and Davis. Also present was Mr. Manzullo.

Chairman Ney. [Presiding.] Good afternoon. The subcommittee on Housing Community Opportunity will come to order. And without objection, all members opening statements will be made part of the record. Hearing no objection they are part of the record. I would remind subcommittee chairs and ranking minority members are recognized for five minutes each. All other members are recognized for three minutes each. And we will alternate, of course, between the majority and minority. I would also want to note due to the length of the time we are going to have to spend and the amount of witnesses, we will try to keep fairly strict on the opening statements to the time so that we can have the opportunity to hear from the witnesses.

This is the first housing subcommittee hearing since I was selected as Chairman. It is my hope that the hearings we conduct in the 108th Congress will be informative and of an invaluable assistance to the members as we contemplate legislation that provides housing opportunities for all Americans. I intend for all the hearings to be fair and balanced, and I pledge to work with Ms. Waters, the ranking member, and all the members to see that this is a very productive subcommittee. And I would note, Ms. Waters and I had a conversation just this past week on communicating with each other throughout this process.

Today's hearing is about the Department of Housing Urban Development's July 28, 2002 proposed rule that attempts to reform the Real Estate Settlement Procedures Act, as we all know as RESPA, which will be the first major reform attempt since 1974. On October 5, 2002, the Financial Services Committee heard testimony from Secretary Martinez. Chairman Oxley and the members have expressed a desire to hear other perspectives on this proposal before it became final. This hearing is a continuation of that process in reviewing the proposed rule by hearing from the many different groups that will be affected by this proposed regulation.

The Committee has invited a broad cross-section of the real estate and mortgage finance industry as well as consumer advocates in an attempt to fully understand this impact of RESPA reform. I think that everyone here shares the intent of HUD in crafting this regulation which is making real estate settlements easier and more transparent for consumers.

Buying a home has become simply too complex and needs to be simplified so there is more transparency in the pricing of settlement services. While we all may agree on that goal, of course, there are a lot of differences on how we are going to achieve that goal. Our witnesses today are here to offer their views on whether or not the proposed rule will achieve that transparency and simplify the home buying process, and if not, what can be done to improve the proposal.

I do look forward to hearing from our witnesses. And I want to take a moment to recognize that because of the size and complexity of the real estate settlement industry, we are unable to accommodate, of course, every group that wanted to come to testify today. We also have some material for the record that we will submit. I know that such groups as the Independent Community Bankers of America and the Appraisal Institute have statements that reflect important segments of the real estate settlement process, and with objection, their statements, as well as those of the Consumers Bankers Association, American Bankers Association, and the National Association of Realtors, will be entered in the record. Hearing no objection, they are entered into the record. Also, without objection, the members will be allowed to submit again their written statements for the record.

At this time I would yield to Mr. Watt.

Mr. WATT. Thank you, Mr. Chairman. I will be very brief. If our ranking member was here and—or if we had other members who had not been here previously to discuss this issue, I probably would just pass, but—actually I will defer to my ranking member since she just walked in. And then I can pass.

You want me to continue or you——

I think I agree with the Chairman that we all think that some procedures that make the buyers more aware of what is happening, and speed up the process, and less complex are desirable, but that the devil is always in the details. And how you get there from here is a very complex issue that, I guess I have probably been dealing with longer than most people on this committee because I practiced law for 22 years doing real estate work before I came to Congress. So that is 22 years plus the 10 years that we have been talking about this on the committee. Thirty-two years I have been working on this issue, and some things that appear to be logical are not necessarily the most logical way to proceed. And some ways that appear to be illogical may be the only way that you can achieve the necessary objectives.

So I will be anxious to listen to all of the people who have input to make on this issue. I think our objectives are all the same, to simplify and make the process more transparent and more visible.

How we get there from here can be a very difficult issue, and I will be looking forward to your suggestions about how you do that.

I did submit a letter to HUD on this issue on the proposed regs and they did not much care for what I had to say, but maybe you all can have some influence, and maybe we can have some influence in this process. So I look forward to it and I will yield back the balance of my time.

Chairman NEY. I thank the gentleman for his statement. And the chair will yield to the ranking member.

Ms. Waters?

Ms. WATERS. Thank you very much, Mr. Chairman. I would first like to thank you for making this such a top priority for the work of the subcommittee. We could not have a more timely or important attempt at reforming and simplifying the home buying process.

I would like to commend HUD for the work that they have done. I know the length of time that HUD has been involved in trying to deal with this reform, and it is not easy. We had a lot of vested interest here from the mortgage brokers to the lenders themselves, and everybody who does loan origination, the real estate interest, insurance interest. And I have noted in the information that I have been given that everybody has got something to say about what is good and what is bad about the proposed reform. And so we are all going to have to work together to see if we can do the best possible job for the citizens of this country.

I need not say to anyone in this room that home ownership is perhaps one of the most important efforts that any citizen can be involved with. This business of home ownership has been referred to as like motherhood and apple pie. We are all told that we should aspire to own a home and we all do want to own a home and should be able to own a home.

And so most people do not pay cash for their home, they have to get involved in a very complicated and sometimes scary system and procedures in order to do that. And we have got to help our citizens be able to have access not only to mortgages, but to be able to feel comfortable that they can sit down with loan originators and others and not be frightened or have the procedure so complicated that they do not understand what is going on.

In all that we do, I think someone mentioned it in their proposed statement here, we must not do anything that will exacerbate the problems that we are trying to straighten out in this committee. Whether it is on the Republican side of the aisle or the Democratic side of the aisle, we are all focused on doing something about predatory lending. And we do not intend to allow anything to happen in this reform process that will make that job more difficult or more complicated.

So I am delighted that you are all here today. I look forward to hearing your testimony. And I am hopeful that we can have a bipartisan effort that will move forth from this committee at the appropriate time, based on all of the information that we have gathered and all that we have come to understand about the process so that in the final analysis, we will be able to serve our constituents and protect our consumers.

So I would like for everybody to make some money, but not at the expense, necessarily, of our consumers.

So, with that, Mr. Chairman, I will turn this hearing back over to you.

Chairman NEY. I thank the ranking member for her statement.

And the gentleman from Wisconsin, Mr. Green?

Mr. GREEN. I thank you, Mr. Chairman, I have no opening statement. I look forward to the testimony.

Chairman NEY. The gentleman from Alabama, Mr. Davis?

Mr. DAVIS. Thank you, Mr. Chairman.

The up side, I guess, of these kinds of hearings is that junior members, like myself, get to question relatively near the beginning. The down side is having to follow Mel Watt and Maxine Waters. So I hope you will take that into account.

I want to welcome all of you today. I have the advantage, I suppose, of being a new member of this committee. I do not have a lot of preconceptions about what took place before I got here.

What I can tell you is as I look at RESPA, first of all, I share Ms. Waters' comment that this is a serious problem and I think that HUD ought to be complimented for trying to get its hands around it.

I would also echo Mr. Watt's comments and the Chairman's comment that all of us, I think, want to see consumers have as much information as possible—no less than that. What none of us want to see is a system that at the end of the day purports to offer a certain level of predictability, but then to see that predictability undone by various definitional ambiguities.

At the same time, none of us want to see a world where the burden is put on consumers—on people that were trying to buy a home for the first time to unravel the process that is already frighteningly complex.

I have a third concern, that I suspect Mr. Watt may have, too—a lot of solo practitioners—a lot of small practice lawyers in this country of ours depend on real estate closings and they depend on the real estate closing business to earn a livelihood. I have a natural predisposition against a system that does not give people a chance to select their own lawyer—that may be the old criminal defense lawyer in me talking, to some extent. But what troubles me about these reforms—and my questions may well be along these lines—deal with the lack of flexibility with individual borrowers—potential homeowners would have in a system which does not necessarily allow them to select their own counsel.

I would agree, as a general proposition, that the interests of people trying to buy a home and people trying to sell it is often an antagonistic one. Certainly a lot of the people who are engaged in the process believe it is an antagonistic one. So I favor a regime, if we can find a way to serve our predictability interests—I favor a regime that would give people more flexibility in selecting counsel of their choice.

But I am eager to learn from you. I am eager to listen to you. And I suspect since not that many of us are here, it will not take that long to do either one of those.

I yield back the balance of my time, Mr. Chairman.

Chairman NEY. I want to thank the gentleman.

Next is the gentleman from Nebraska—Mr. Bereuter?

Mr. BEREUTER. Thank you, Mr. Chairman—no opening statement.

Chairman NEY. Thank you.

The gentleman from North Carolina, Mr. Miller?

Mr. BRAD MILLER. No opening statement—I am struck by how diverse the perspectives are with the witnesses and I look forward to hearing the testimony.

Chairman NEY. The gentlelady from Florida?

Ms. HARRIS. No opening statement, Mr. Chairman. Thank you.

Chairman NEY. What an easy committee.

The gentleman from Connecticut?

Mr. SHAYS. Mr. Chairman, just to thank you for holding these hearings and thank our witnesses—no statement.

Chairman NEY. And the gentleman from Pennsylvania?

Oh, the gentleman from Illinois, Mr. Manzullo?

Mr. MANZULLO. Thank you, Mr. Chairman, for the opportunity to provide a statement at today's hearing. I am a member of the Financial Services Committee, but not of this subcommittee.

Without a doubt, the residential real estate market is a bright spot in our otherwise uneven economy. HUD's proposal to revise the regulations governing the residential real estate settlement process is ambitious, it is complex and it is rushed.

While I support simplifying the process so that more first-time home buyers could enter the market, I believe that HUD's rush to finalize its proposal jeopardizes our real estate market in the short term. In addition, if adopted, it will make fundamental and perhaps irreversible changes to the process that may undermine the long-term goals of providing affordable housing and consumer benefits within a residential real estate market.

I believe that HUD has not—N-O-T—HUD has not fully analyzed and carefully deliberated all the critical issues from this proposal. Specifically, HUD has not thoroughly considered the economic effects of the proposal on small businesses, a very important segment of our community—of our economy.

Pursuant to the Regulatory Flexibility Act and Executive Order 12866, HUD attempted to undertake an economic analysis of the proposal and its effect on small businesses. While the 98-page document summarizes and highlights many elements of the proposal, HUD has failed to adequately determine the economic effect on segments of the small business community. HUD readily admits the small business community may lose anywhere from $3.5 billion to $6.3 billion annually. However, HUD does not break down the costs to each segment of the industry. HUD does not even include all the industries impacted.

There is no detailed economic analysis for the community banks, small real estate agents, small title agencies—just to name a few, along with the other small businesses.

As chairman of the Small Business Committee, I am going to be holding a hearing on HUD's regulatory flexibility analysis to determine why this organization cannot simply follow the law.

Ms. Velazquez, who is my ranking member on the Small Business Committee, is opposed to this proposal. The Small Business Administration, through Tom Sullivan, chief counsel for advocacy, is opposed to this proposal because HUD has not, Mr. Chairman, followed the law.

In fact, if you take a look at their proposal, they attempt to do in 88 pages a $6 billion economic analysis. And HUD should hang its head in shame over having all the resources and not being able to simply determine the groups that are involved.

As a practitioner of law for 22 years—the same as Mr. Watt—and someone who has been through over a thousand real estate transactions, this is not a new area to me. But I can assure you of this—if this goes through, Mr. Chairman, you could find this entire industry will be tied up by five or six major lenders across the country, creating one of the largest monopolies and smoking all the small businesses in the country.

I would call your attention to page 63 of the report that says, "Summary of Small Businesses Impacted and Alternatives Considered"—all they had to say is that because you have third party providers out there they could participate and be a part of these large conglomerates. I mean, it is such a naivete that they will get smoked simply because they are not big.

Chairman NEY. I want to thank the gentleman. The time of the gentleman has expired.

An opening statement, if Mr. Baker wishes, from Louisiana?

Mr. BAKER. Thank you, Mr. Chairman. I have no statement at this time.

Chairman NEY. I want to thank the gentleman.

We will move on to introduction, quickly, of the witnesses and then we will move on to the panel.

I want to thank all of the witnesses for being here today.

First is John Courson. Mr. Courson currently serves as Chairman of the Mortgage Bankers Association of America. The Mortgage Bankers have a membership of approximately 2,600 companies, including all elements of real estate finance, mortgage companies, mortgage brokers, commercial banks, thrifts, life insurance companies, as well as others in the mortgage lending field.

Mr. Courson also serves as the CEO of Central Pacific Mortgage Company, which is headquartered in Folsom, California.

Margot Saunders—Ms. Saunders serves as the managing attorney of the National Consumer Law Center, NCLC; provides support training and technical assistance for legal professionals in the areas of consumer fraud, debt collection, finance law and home ownership programs. Ms. Saunders duties include representing low-income clients on financial credit issues and analysis of water and energy issues as they affect low-income people.

She has recently completed terms on the Federal Reserve Board's Consumer Advisory Council and the American Waterworks Association Public Advisory Forum.

Stanley Friedlander—Mr. Friedlander is the President of the American Land Title Association and the past President of the Ohio Land Title Association. He is the Co-founder and President of the Continental Title Agency Corporation, headquartered in Cleveland, Ohio.

It is a little warmer in D.C.—not much—than Cleveland this morning.

Anne Canfield—Anne Canfield is Executive Director of the Consumer Mortgage Coalition, known as CMC, a trade association representing national mortgage lenders, servers—servicers and service providers. Ms. Canfield is also President of Canfield and Associates, Incorporated.

Neill Fendly—Mr. Fendly currently works with Camelot Mortgage, Incorporated, an Arizona-based mortgage company, and has been involved with the National Association of Mortgage Brokers as a member of the board of directors before serving as Vice President elect and President of NAMB.

He is currently the Government Affairs Chair for NAMB and was a member of the federally mandated mortgage reform working group.

D. Russell Taylor—Mr. Taylor is the first Vice Chairman of America's Community Bankers. He has been a member of ACB's board of directors since 1998. Members of ACB originate more than 25 percent of all mortgages in the United States and significantly more than half of all mortgages originated by depository institutions.

Mr. Taylor also serves as a member of the New Jersey League Community and Savings Bankers and is a member of the Government Affairs Counsel on Legislative and Regulatory Committee. He is currently the President and CEO of Rahway Savings Institution in Rahway, New Jersey.

And F. Gary Garczynski—Mr. Garczynski is the immediate past President of the National Association of Home Builders. He is testifying today for C. Kent Conine, NAHB's current president, whose flight to Washington from Dallas was canceled.

Mr. Garczynski is President of the National Capital Land and Development Company in Woodbridge, Virginia. In the past 30 years, he has built over 4,000 homes in the greater Washington metropolitan area. He has served on the executive committee of NAHB since 1993 and on the Virginia Housing Study Commission since 1995. He was also an appointee to Virginia's Commission on Population and Growth.

I want to thank all of the witnesses for your important testimony today.

And without objection your written statements will be made part of the record. You will each be recognized for a five-minute summary of your testimony.

And we will begin with Mr. Courson.

STATEMENT OF JOHN A. COURSON, CHAIRMAN, MORTGAGE BANKERS ASSOCIATION OF AMERICA, WASHINGTON, DC

Mr. COURSON. Good afternoon. Thank you for inviting the Mortgage Bankers Association to participate in these hearings.

Mr. Chairman, I would like to just state up front that the Mortgage Bankers Association does stand behind Secretary Martinez' bold and far-reaching proposal to reform the mortgage disclosure system.

I have been in this business—many would say too long, but over 40 years. And throughout those 40 years, the one consistent thing that I have seen is the growing amount of paperwork, numbers, calculations and confusion that has built up and seems to build every year as we move through the genesis and development of the mortgage lending process, a process that, through those numbers and that myriad of paperwork has tended only to fool and mislead borrowers and certainly add confusion to an already confusing transaction.

So we, at the Mortgage Bankers Association, commend and applaud Secretary Martinez for really stepping up to the plate and putting forth a proposal—a far-reaching proposal that would, in fact, address the complexity and confusion in the mortgage lending process.

Through the introduction and the concept of a guaranteed fee package, the proposal has put forth a rule that would, in fact, simplify—would, in fact, take some of the mystery, some of the detail and some of the confusion out of this existing disclosure system.

As you know, the Guaranteed Package, obviously, is a package that contains two components—a lump sum of the cost to close the loan and an interest rate. We, at MBA, are very confident that HUD's package has three very important objectives to it. The first, it simplifies the process of mortgage—of the mortgage disclosure systems. Secondly, it certainly provides consumer certainty. And it will foster and does foster competition.

And, Mr. Chairman, just let me say, again, simplification, certainty and competition—let me just talk for a minute, if I may, about simplification. I have talked about the complexity of the process not only from the consumer standpoint, but those of us who are practitioners who originate loans. Through the guarantee fee package arrangement, we are able to give the consumer a single price and an interest rate that is more clear and clearly more simple than trying to pour through a list of charges that are very confusing and, frankly, the purposes of which are unknown to many consumers.

Secondly, the certainty—the consumer now will have, with certainty, a price that he or she can shop effectively to determine that they are getting the best deal for them.

And, of course, lastly, fostering competition because with this process, we will be able—and they will be able to negotiate and go to lenders—go to originators and shop for the best transaction and create competition in a marketplace that, today, really is forestalled by virtue of the fact of the complexity.

Obviously, we have submitted our comments to the department for some areas where we think there can be improvement and modifications. But let me say that we do believe that the Secretary—and I applaud the Secretary for being on the right track.

Before I close, Mr. Chairman, though, I would like to say one other thing. There has been a lot of conversation in past weeks and months about the negative impact of this rule on small businesses and the fact that small lenders will, in fact, be disadvantaged and large lenders will replace them as effectively being able to compete.

MBA dissents from that view and we can speak, frankly, with some certainty in that more than 50 percent of our members are small, midsize lenders. We compete today. There are large lenders out there that are better capitalized, have lower cost of funds, have affiliated a business arrangement and have the wherewithal, clearly, that many of us who are small and midsize lenders do not have, but yet I will tell you that we compete effectively in this marketplace.

Actually I look at it and say that this proposal gives us a better opportunity to compete. We now can enter into co-ops, affiliations, alliances that allow us to become part of groups that we assemble services to provide to the consumer to more effectively compete in the marketplace. So I would tell you—I would say to you that our members are competing today against the same lenders that will be there after this rule is passed. And we think, in fact, we can effectively compete.

So I thank you and I appreciate the opportunity to testify before this committee.

[The prepared statement of John A. Courson can be found on page 158 in the appendix.]

Chairman NEY. Well, I thank the gentleman for his testimony. Ms. Saunders?

STATEMENT OF MARGOT SAUNDERS, MANAGING ATTORNEY, NATIONAL CONSUMER LAW CENTER, WASHINGTON, DC

Ms. SAUNDERS. Thank you, Mr. Chairman. I appreciate the opportunity to be here today. I testify on behalf of the low-income clients of the National Consumer Law Center, as well as the Consumer Federation of America, Consumers Union and U.S. PIRG.

We wish, also, to commend Secretary Martinez for the dramatic approach to RESPA reform advocated in these proposed rules. The stated goals of the rules and the orientation are wonderful to protect consumers. We credit the hard work and the creativity of the HUD staff in the conception of the rule and we think that many of the ideas in the rules are constructive.

There are several overarching concerns and a myriad of important details that we believe must be worked through to ensure that the rules do, in fact, protect consumers. And we have provided 47 pages of comprehensive comments to HUD to facilitate that.

However, we want to make absolutely clear that our most important concern is that this rule not be allowed to facilitate predatory lending. And we have that concern because the Guaranteed Mortgage Package, which is the subject of so much of the debate, will have the effect of hiding the Truth in Lending Disclosures that are required in most mortgages today. The impact of that cannot be understated for agency and consumer enforcement of the single most effective and important consumer protection law that we have on the books affecting consumer mortgages.

As a result we—and, now, this is a broad coalition of consumer and legal services programs across the country—have strongly advocated to the Secretary that if he moves forward with the Guaranteed Mortgage Package that he exclude from it all subprime loans. They have proposed excluding all HOEPA loans. That is not a broad enough category because the impact of the Guaranteed Mortgage Package would be to allow many loans which would otherwise be counted as HOEPA loans to be included in the guarantee and we would have no way of determining if, in fact, it was a HOEPA loan. By HOEPA, I mean the Homeownership Equity Protection Act, which is the federal law designed to protect against predatory lending.

There are three main aspects to the rule. One is the Guaranteed Mortgage Package. The second is the change in the disclosures of the yield-spread premiums charged by brokers. And the third is the rule's proposal on how to deal with Good Faith Estimate disclosures.

The Guaranteed Mortgage Package, we think, has a lot of good ideas and we support it, so long as it, in fact, is a guarantee of both closing costs and points and interest rate. That is crucial. If you allow someone to buy a package of services without also buying the interest rate, it is like buying the wheels on a car without buying the car. And those wheels are only going to go on certain cars. In fact, you are tied into certain loans without knowing what the price for the rest of the loan package will be.

The yield spread premium proposal that HUD has made is very good. Essentially for the first time, HUD is actually requiring that consumers be given the benefit of the fee that the lender is paying to the broker. And since the fee the lender is paying to the broker is reflected in the interest rate that the consumer pays, the consumer should have control over how that fee is applied.

In the amount of time I have now, I cannot go into the complexities here, but while we do support the proposal, we must point out that to make this proposal effective, it must be included in those parts of the regulations that deal with yield spreads, which are enforceable. It cannot just be included in those parts of the regulation which deal with disclosures, which are not privately enforceable.

Thirdly, HUD has proposed that the information that consumers received on the Good Faith Estimate when they first apply for a loan actually be true information and that there be small tolerances between the amount of money that the lender says is going to be charged and the amount of money that is actually charged for closing costs when the consumer gets to closing. We support these proposals and think they are very, very good.

And, in sum, I am happy to answer any questions. We have worked extensively with HUD in the hopes that they will continue with some parts of this rule and guard against facilitating predatory lending in other parts.

Thank you.

[The prepared statement of Margot Saunders can be found on page 400 in the appendix.]

Chairman NEY. Thank you for your testimony.

Mr. Friedlander?

STATEMENT OF STANLEY B. FRIEDLANDER, PRESIDENT, AMERICAN LAND TITLE ASSOCIATION, WASHINGTON, DC

Mr. FRIEDLANDER. My name is Stanley Friedlander. I am the President of Continental Title Agency located in Cleveland, Ohio. I am appearing today as President of the American Land Title Association, which represents both title insurance companies and over 1,750 title insurance agents, most of which are small businesses like mine.

ALTA, and I, personally, would like to thank you for holding these hearings. We understand the concerns—that many have prompted the HUD proposed regulations and believe that the Secretary and the Department deserve credit for the boldness of their initiative.

However, the HUD proposed rules could have a very negative impact on our residential real estate market. We believe the rules proposed by HUD do not serve the interests of the consumers of our products and services; would adversely affect competition in our business; and will particularly hurt the small businesses that are the cornerstone of our industry.

HUD is proposing to replace the current regime with two alternatives. The first is a revision of the current Good Faith Estimate regime. The second regime HUD proposes would encourage mortgage lenders to offer what HUD refers to as a Guaranteed Mortgage Package, which would contain essentially all of the loan and other real estate-related settlement charges at a single guaranteed price, together with a loan at a guaranteed interest rate.

We have serious concerns about these proposals and I will highlight an alternative we have recommended to HUD that would achieve many of the agency's objectives, while minimizing consumer and industry problems. We urge the committee to ask HUD to seriously consider this alternative.

The HUD-proposed regimes would pose particular problems for consumers in purchase sale transactions, as opposed to refinance transactions. In those transactions, the buyer and the seller have separate interests from the lender in the nature and the quality of the title services required. Under the HUD blind package proposal, the consumer will not know the services that they are obtaining or the individual costs. And, therefore, will not be able to compare packages.

In addition, in a home purchase, the buyer and the seller may already have agreed on the selection of the provider of the title or closing services before the buyer has even begun to shop for a mortgage.

As the price of the Guaranteed Mortgage Package might also include these services, the borrower could end up paying twice for the same service. Further, in most areas of the country, as in Ohio, the seller generally pays half the costs of closing or a significant portion of the title insurance charges and government transfer and deed recordation charges. The HUD proposals tilt heavily in favor of the packaging alternative, because packagers are provided an exemption from the Section 8 of RESPA.

As a mortgage loan at a guaranteed interest rate must be a part of the Guaranteed Mortgage Package, therefore only lenders will effectively be able to offer packages. This will have a particularly adverse consequence for our small businesses.

HUD has structured its GMP proposal in a way that mortgage lenders are in a position to realize greater profits on the Guaranteed Mortgage Package prices by negotiating lower prices from the providers of the service packages and will, themselves, pick up a packaging fee. Smaller abstractors and title agencies will not have the resources to be able to offer the kinds of prices that the larger company can provide and still be able to provide the quality of services required. Accordingly, these smaller businesses will have a difficulty competing for the consumers' business and surviving.

We believe the two-package approach will allow lenders and others to package on a local level. It will take into account local costs, local needs and allocations that allow customization. We suggest that the HUD proposal be modified to adopt a Guaranteed Mortgage Package which would consist of a loan at a guaranteed interest rate and then all lender-related services as one charge and, in addition, a guaranteed settlement package. That could be offered by any party—by title insurers, agents, real estate brokers, lenders, escrow companies or attorneys. That would guarantee a single price for the settlement charges and they would include title and related charges, government recording and transfer charges and charges required for closing purposes.

We believe this two-package approach would better achieve HUD's goals of ensuring price certainty in the settlement process for the customers and injecting significant shopability—price competition in both the lending and the settlement industries.

Please also note that irrespective of whether one believes that HUD's proposals are good or bad, or workable or unworkable, this Committee and the Congress should be concerned about HUD's implementing such a change without clear legal authority.

I thank the committee for the opportunity to participate in this process. And we encourage HUD to move slowly and carefully on this proposal.

[The prepared statement of Stanley B. Friedlander can be found on page 239 in the appendix.]

Chairman NEY. I thank the gentleman for his testimony.

Ms. Canfield?

STATEMENT OF ANNE C. CANFIELD, EXECUTIVE DIRECTOR, CONSUMER MORTGAGE COALITION, WASHINGTON, DC

Ms. CANFIELD. Thank you, Mr. Chairman for the opportunity to testify. The Consumer Mortgage Coalition is pleased to be here today.

We would like to submit a copy of our full statement and comment letter that we submitted to HUD for the committee record if that is possible.

Chairman NEY. Yes, without objection.

Ms. CANFIELD. Thank you.

The CMC believes HUD's proposal represents a major step toward improving the process by which consumers obtain mortgage loans in this country. Significantly, it gives loan originators and other settlement service providers the option of guaranteeing closing costs to consumers. And if such a guarantee is provided, it allows packagers to use their purchasing leverage to lower these costs—something which RESPA, to date, has prohibited.

With this guarantee, consumers will have a better understanding of closing costs and be better able to shop for the best loan that suits their needs. We also believe that this guarantee, which the proposal calls a "Guaranteed Mortgage Package" or a "GMP," if structured properly, will help reduce predatory practices.

The CMC has developed a comprehensive set of proposals to address predatory lending, which are in Tab 1 of our comment letter to HUD. The GMP is an important element of those proposals for two reasons. First, the proposal will ensure that consumers receive relevant information about a loan's costs early in the process, which promotes comparison-shopping. Second, by simplifying the comparisons, it will increase consumer understanding and make more difficult the deception that characterizes abusive loans.

I would like to focus today on five key aspects of HUD's proposal that we believe are crucial to this rule becoming a reality—not just the reality of becoming a final rule, but the reality of millions of borrowers obtaining lower cost loans as a result of receiving offers of guaranteed mortgage packages.

First, the structure of the Guaranteed Mortgage Package—HUD has included in the GMP the guaranteed settlement costs and an interest rate component. Although the proposal calls this an "interest rate guarantee," the interest rate is not, and cannot be, a guaranteed rate, unless the borrower locks in the rate and qualifies for the loan. The costs to the consumer and the industry of actually offering every applicant a guaranteed rate would be staggering. HUD understands this.

Because they are not guaranteed, we have urged that the interest rate and any discount points which together constitute the interest price of the loan be separated from the guaranteed closing costs package. Consumers need to receive, and shop with, offers of guaranteed settlement costs. These costs, far more than the interest rate, are misunderstood and are not subject to comparison-shopping and come as unwelcome surprises to borrowers at the closing table.

Also, if the interest price were removed from the package, non-loan originators will be more readily able to assemble and offer a guaranteed package because they would not have to offer the actual loan, an act that requires special licensing authority.

If HUD determines to include an interest rate component in the GMP, it must be a conditional rate, subject to underwriting. HUD also wants borrowers who have either not yet accepted a GMP offer, or have accepted but not locked in the rate, to be able to track the rate using some verifiable index. This is a problem, however, because there is no universal index that can be used to track lenders' rates.

Because loan pricing is highly company-specific and is driven by numerous internal and external factors, the only way for this to work is to require that loan originators make their rates available to these applicants on a daily basis, by phone, on a Web site or via some other medium. This will assure that similarly situated borrowers will be treated alike.

A few trade associations, as my colleague just mentioned, have urged HUD to adopt a two-package approach to the rule. One package would be the loan package, including the interest rate and any separate settlement charges imposed by the lender, such as loan origination or loan processing or underwriting fees. The second package would be a settlement package, which presumably would include the remaining settlement costs, such as title insurance, closing attorney, survey, et cetera. It is not clear where the costs for the appraisal or credit report would go. In some proposals, there would be a Section 8 exemption for the services within each package, but not across the packages.

After looking closely at this approach, we cannot support it because it significantly complicates the origination process and raises more questions than it answers. Consumers want simplified shopping. They understand and shop for the interest rate, and they understand that they can raise or lower the rate with discount points. They now need a simple way to compare and shop for closing costs. Having certain closing costs in one package and other closing costs in another package makes it harder, not easier, to shop for these costs.

The structure we see working best is one in which lenders and other settlement service providers may assemble and offer packages of guaranteed settlement costs.

Second, the treatment of HOEPA loans—this proposal excludes from the exemption for packaging loans subject to the federal HOEPA, which applies to loans whose rate and points exceed specific thresholds. We strongly disagree with this exclusion. We think it is wrong to withhold from subprime borrowers the clear shopping and cost-saving advantages of obtaining GMP offers. It has been argued that many HOEPA borrowers today do not shop effectively for loans. That is all the more reason to include them under this rule. We need to give them every tool and motivation to shop. In fact, HOEPA borrowers are likely those most in need of GMP offers. Armed with guaranteed settlement cost offers, HOEPA borrowers can focus on obtaining the best loan price for the loan available to them in the market—price being the interest rate and the points.

Third, federal preemption—many state laws conflict with or frustrate the purpose of the HUD proposal. There are state laws that require the disclosure and itemization of all closing charges. There are other state laws, like Section 8, that—like Section 8 prohibit referral fees, or that require a direct pass-through of all third party closing charges to providers—of settlement—third party charges to consumers. An exemption from Section 8's federal prohibitions and the express federal authority to bundle and guarantee settlement costs, will have——

Chairman NEY. I am sorry to interrupt—I would have to note that the time has expired if you want to——

Ms. CANFIELD. Okay.

Well, I was going to say that preemption is important—HUD has the authority to issue the rule with preemption. We would encourage them to do so, so that the Guaranteed Mortgage Package can actually work.

And finally, as noted by some—by my colleagues here to my right, there are significant changes in the Good Faith Estimate. We have encouraged HUD to delay those changes in our proposed comment letter for two reasons. One is that if it became a requirement, all of our lenders would have to focus on implementing those mandatory changes, which would take up to 18 months, and delay doing the Guaranteed Mortgage Package.

The second is that HUD's legal authority in this area is a little bit questionable. And it would delay—it might—pending lawsuits might delay the whole rule for years.

[The prepared statement of Anne C. Canfield can be found on page 69 in the appendix.]

Chairman NEY. Thank you for your testimony.

Ms. CANFIELD. Thank you.

Chairman NEY. Mr. Fendly?

STATEMENT OF NEILL FENDLY, CHAIR, GOVERNMENT AFFAIRS COMMITTEE, NATIONAL ASSOCIATION OF MORTGAGE BROKERS, WASHINGTON, DC

Mr. FENDLY. Chairman Ney, Ranking Member Waters, members of this subcommittee, I am pleased to be here and appreciate the opportunity to discuss HUD's proposal to reform RESPA.

Today, mortgage brokers originate more than 60 percent of all residential mortgages and are the key to bridging the gap in minority home ownership, based on a recent study. A mortgage broker does not simply press keys and provide the customer with a loan, but instead, serves the role of adviser, credit counselor, underwriter and personal contact to the consumer. Brokers also provide lenders a nationwide distribution channel that is less expensive than traditional lender branch operations.

We support the administration's goal to increase home ownership and HUD's stated goals of simplifying the mortgage process, but this rule achieves just the opposite. The proposed rule is unworkable in the real world for both industry and consumers, will harm small businesses and the mortgage broker industry, in particular.

In our comment letter, NAMB provided HUD with a sample Good Faith Estimate form. Our proposal will strengthen, simplify and clarify the disclosure of costs provided to consumers in advance of settlement and give consumers a true comparison of the costs of a mortgage loan.

NAMB has many concerns with HUD's proposed rule, but the single most important issue is HUD's re-characterization of yield spread premiums. The characterization of a yield spread premium is a lender payment to the borrower for a higher interest rate trades and ambiguity in the marketplace that will not only confuse borrowers, it negates HUD's own 1999 and 2001 statements of policy, which define a yield spread premium as a payment for goods, facilities or services actually furnished or services actually performed for the lender, as well as the borrower.

Mortgage lenders save millions of dollars in facilities and employee costs by originating loans through mortgage brokers. Yield spread premiums help pay the day-to-day broker operations. HUD's re-characterization of a yield spread premium ignores lender payments to the mortgage brokers for the facility that the broker provides to the lender.

In addition, this re-characterization will lead to a new round of class action litigation, as borrowers will be confused as to the function of a yield spread premium and will ask at closing, "Where is my check?" The class action plaintiffs bar will seek these consumers out, causing another wave of class action lawsuits for the industry, which will only increase the costs to the consumer.

The proposed rule also creates an artificial and competitive disadvantage for the mortgage broker industry. By regulating that the broker include the yield spread premium in the calculation of net loan origination charge, but not including the same for all originators, HUD is complicating the real estate settlement prices—process. The consumer is unable to do a true apple-to-apple comparison of the cost of the mortgage.

This proposed rule will also prohibit a mortgage brokers' ability to advertise a no-point loan, even though our competitors will be allowed to do so. A broker and a lender might charge a consumer the same rate and cost for a mortgage loan, but if both receive indirect compensation, only the broker must show this as direct compensation. Thus, for the very same loan to the consumer, a broker cannot advertise this loan as a no-point loan and will appear less competitive.

Under the proposed rule, many mortgage brokers will no longer be able to originate FHA and VA insured mortgage loans. Direct compensation is limited, by regulation, to 1 percent on these types of loans.

In the proposed rule, indirect compensation is artificially transformed into direct compensation and subject to the cap. If brokers cannot charge enough to cover their costs for these types of loans, brokers will be forced out of the VA and FHA lending industry. This is significant as approximately 31 percent of all FHA insured mortgage loans are originated by mortgage brokers.

This proposed rule was not built on a solid foundation of market realities, but, instead a fundamental misunderstanding of such realities due to its flawed economic analysis. Constructing the rule based on inaccurate analysis will lead to a flawed rule that will cause great harm to consumers and could have devastating repercussions in a $2 trillion housing market.

The SBA has requested that HUD issue a revised analysis that takes into consideration the comments of affected small entities and develops regulatory alternatives to achieve HUD's objectives while minimizing the impact on small business. Even the FPC said the disclosure of both compensation contained in the proposal could confuse consumers and lead them to misinterpret the overall costs of a transaction and that it might inadvertently burden consumers and competition.

NAMB believes HUD has significantly underestimated the regulatory burden of its proposed rule. HUD admits the proposed rule would increase the regulatory burden by 2.5 million burden hours, which is the equivalent of 289 years. Such a huge burden will increase the cost of credit to consumers.

NAMB sincerely appreciates the opportunity to share our concerns with you on HUD's proposed rule to reform RESPA. We respectfully request that the subcommittee and the Financial Services Committee work with HUD to ensure that any finalized rule actually achieves HUD's stated goals of providing clarity and simplification to the consumer, while not providing further confusion or complexity to the marketplace.

In achieving this goal, HUD must ensure that credit remains available for consumers and is not compromised.

Thank you.

[The prepared statement of Neill Fendly can be found on page 168 in the appendix.]

Chairman NEY. Thank you.

Mr. Taylor?

STATEMENT OF D. RUSSELL TAYLOR, CHAIRMAN, AMERICA'S COMMUNITY BANKERS, WASHINGTON, DC

Mr. TAYLOR. Thank you.

Chairman Ney, Ranking Member Waters, Members of the Subcommittee, thank you for this opportunity to be here today and testify on this important issue.

My name is Russ Taylor. I am the President and the CEO of The Rahway Savings Institution, which is located in Rahway, New Jersey. We are a New Jersey state chartered mutual savings bank, founded in 1851. We have $430 million in assets. And our primary business is one to four family residential mortgage lending.

Today I have the honor and the privilege of testifying as Chairman of America's Community Bankers. ACB member banks originate more 25 percent of all mortgages originated in the United States and significantly more than half of all mortgages originated by depository institutions. In our members operate a large number of mortgage banking affiliates that originate a substantial part of the business from the segment of the industry.

Thank you for this opportunity to testify today on RESPA reform.

Mortgage process mandates are extremely burdensome, costly and confusing for consumers and lenders. Reform is long overdue. ACB is pleased that Secretary Martinez has taken an important step forward in this issue. But changes must be implemented with careful deliberation and with a sufficient transition period consistent with the cost of compliance.

ACB generally supports the concept of the Guaranteed Mortgage Package and the proposal to require mortgage broker disclosures. However, we strongly urge HUD to reconsider making changes to the Good Faith Estimate contemporaneously with introduction of the Guaranteed Mortgage Package. We believe that making all of these changes at the same time would unnecessarily disrupt the mortgage market.

ACB strongly supports HUD's efforts to require disclosure of mortgage broker fees and believes this requirement should be implemented immediately. Mortgage broker disclosure is essential to preventing possible abuse of yield spread premium payments. We do not believe that potential delays in other elements of HUD's proposal should delay this new requirement.

ACB supports the option of Guaranteed Mortgage Package, but we strongly believe that the current Good Faith Estimate must remain a viable alternative for those lenders who do not wish to package or who are unable to do so. It is simply too dangerous to dramatically change Good Faith Estimate procedures while simultaneously launching the potentially revolutionary Guaranteed Mortgage Package.

ACB believes that small to medium-sized lenders are an integral part of the mortgage process and it is imperative that they be able to use the packaging option to the extent that they wish. We believe that many community banks will be able to work with local service providers to offer an attractive package. It may be that the optimal way for smaller institutions to participate in the packaging option may be to use larger third parties to coordinate or provide the Guaranteed Mortgage Package. In this case, we support restrictions in the ability of GSEs to offer packages and regulation to prevent loan steering by third party packagers. Without such regulations, the full competitive benefits of RESPA reform are unlikely to be realized.

The proposed Guaranteed Mortgage Package, arguably, would provide customers an easy method of comparison-shopping. However, we are concerned that providing a so-called interest rate guarantee that is held open for a minimum of 30 days as part of the package would just not work. Problems arise because it is not a true interest rate guarantee. And the length of commitment is beyond industry norms. We suggest that HUD work with lenders to develop a methodology for establishing and adjusting rates.

Another concern is conflict with state law. There are approximately 40 states in which the Guaranteed Mortgage Package may not be able to be implemented for a variety of reasons. ACB suggests that HUD look at the differences in how closings are conducted from state to state and at what different state laws may require.

In conclusion, ACB believes that—one, mortgage broker fee disclosures are an integral part of making mortgage fees comprehensible to consumers and should be implemented immediately. The Guaranteed Mortgage Package, with revisions, should take priority and be tested in the market as soon as practicable. And finally, revisions to the Good Faith Estimate should be postponed, re-examined and adjusted as the Guaranteed Mortgage Package is being tested.

ACB members stand ready to work with the members of the committee and HUD to complete the RESPA reform process in an effective manner.

We thank you for the opportunity to testify on this issue today.

Thank you, Mr. Chairman.

[The prepared statement of D. Russell Taylor can be found on page 418 in the appendix.]

Chairman NEY. Thank you.

Mr. Garczynski?

STATEMENT OF F. GARY GARCZYNSKI, PAST PRESIDENT, NATIONAL ASSOCIATION OF HOME BUILDERS

Mr. GARCZYNSKI. Chairman Ney, Vice Chairman Green and Members of the Committee, on behalf of the 212,000 member firms of NAHB, I am pleased to have this opportunity to testify in support of HUD's proposal to reform RESPA.

NAHB's comments today will focus on two major components of HUD's proposal. First are the changes in the disclosure requirements of the cost of mortgage transactions to the consumer—the Good Faith Estimate. Second, I want to comment on the addition of an option for lenders to offer a package of settlement services at a guaranteed cost—the Guaranteed Mortgage Package.

NAHB applauds HUD's efforts to increase the transparency and simplify mortgage transactions and loan closings by improving the disclosure of mortgage fees and expenses to consumers. The proposed changes should also eventually lower mortgage transaction costs and help minimize unexpected charges at the time of loan settlement.

My oral statement will be confined to those aspects of the proposed rule which deal with the circumstances involved in processing mortgages for newly built homes. Transactions for newly built homes are different in that they typically involve a fairly lengthy loan origination process that matches a sometimes lengthy building process.

On the Good Faith Estimate, under the requirements for the estimate, the proposed rule does not specify when changes in the transactions warrant a new disclosure. Re-disclosure could be burdensome to lenders in a new construction environment where the loan origination period spans from housing start to home completion and may last anywhere from four months to nine months or more. Many changes can, and normally do, take place during the construction process. For example, the purchase price may fluctuate, depending on the buyer's optional preferences. Also, the attractiveness of different mortgage products may change, as could the buyer's financial situation.

Changes in the home purchase price directly impact the cost of document stamps, transfer tax fees. And similarly, changes in the loan amount affect the fee charge for the lender's title insurance. On the Guaranteed Mortgage Package—the concept of the Guaranteed Mortgage Package is appealing and could reduce consumer costs primarily through originator's negotiations with settlement services that are provided.

However, a guaranteed package that is determined at loan commitment and lasts until settlement on a new home transaction puts the packager in a position of excessive risk. This may lead the original packager to offer less competitive terms than packagers who have an opportunity to offer a mortgage package closer to the date of the projected loan closing. Wider tolerances in guarantees would be needed for a new home transaction where the price and loan amount often change dramatically during the construction period.

So NAHB recommends for financing quotes on newly constructed homes that both the Good Faith Estimate and the Guaranteed Mortgage Package have an alternative that is based upon a days-until-closing threshold for providing final quotes and guarantees. For example, a lender would provide preliminary estimates at the initial application and then issue final guaranteed estimates 30 or 60 days out from the proposed closing. This procedure would be comparable to the timing of guarantees that would be made in financing an existing home purchase.

The solution would allow the customer sufficient time to shop again if the final package was deemed to be less than competitive, while providing the lender an opportunity to adjust those components of the package that actually changed.

In closing, NAHB recognizes the effort HUD has put into correcting some salient shortcomings in an otherwise effective housing financing system. However, loans for new homes, which represent more than a quarter of the annual purchase mortgage originations, have unique characteristics and, thus, they must be specifically addressed in any RESPA reform package. We are confident that HUD will address the concerns that have been expressed regarding this proposal and can do so without sacrifice to mortgage services.

Thank you.

[The prepared statement of F. Gary Garczynski can be found on page 325 in the appendix.]

Chairman NEY. I want to thank the panel for their testimony.

One question I have for anyone on the panel that would like to answer it—under the proposal, loan originators offering loans whose rate or points trigger the HOEPA protections may not benefit from the Section 8 exemption. Should the packaging proposal be extended to HOEPA? And if not, what is the lender's incentive to offer a guaranteed package?

Would anybody like to comment on that?

Ms. CANFIELD. We believe, and stated in our testimony, that the Guaranteed Mortgage Package proposal should be extended to HOEPA loans and they should be included. Without it, there is—HOEPA borrowers are not going to be able to get the benefit of the Guaranteed Mortgage Package offer.

Chairman NEY. I assumed you would want to respond, Ms. Saunders.

Ms. SAUNDERS. That is right, Mr. Chairman. I appreciate the opportunity.

Because the effect of the package will be to hide Truth in Lending Disclosures and it will be impossible to determine whether a lender has complied with Truth in Lending when a package is offered, we think that it is very important to preserve Truth in Lending Compliance for all loans which are not of the most competitive nature. And there can be no debate, I think, that some subprime loans are predatory. To avoid spreading the problem of predatory loans, we need to at least maintain the current transparency, not add to the murkiness of the situation.

So we think that, at least at the beginning part of the process, the Guaranteed Packages should not be allowed not only to HOEPA loans, but to all subprime loans.

Mr. COURSON. Mr. Chairman?

Chairman NEY. Thank you.

Mr. Courson?

Mr. COURSON. I am sorry—if I may——

Chairman NEY. Yes.

Mr. COURSON. In due respect, the system under the proposed rule of the guaranteed fee package—Guaranteed Mortgage Package does not obviate the need to still provide a Truth in Lending Disclosure at the time of the closing of the loan. So, in effect, the borrower will still receive a Truth in Lending Disclosure disclosing those charges that are in the finance charges and the amount financed and an APR, in addition to the Guaranteed Mortgage Package disclosures.

There will be two disclosures. And the TILA, if you will—the Truth in Lending—will still be provided as it is today.

Chairman NEY. Thank you.

One other question I would have, I think, for Ms. Canfield—there is currently at least four national lenders offering one-fee loan products—an example would be ABN AMRO. Since lenders are doing this without a Section 8 exemption, why is there a need for a regulatory change because they are doing it without Section 8 exemption?

Ms. CANFIELD. First, I would make the observation that there are tens of thousands of loan originators out there and only four that are offering any kind of product similar to what we are talking about. But the difference here is a timing difference. Under the HUD proposal, HUD is saying that you will get the Section 8 exemption if you guarantee closing costs at application and send out the guarantee in writing to consumers within three days. For the products that I have seen out there in the marketplace today, their guarantee does not come until much later in the loan—in the loan process—really almost near loan commitment, after the loan has been underwritten and the property has been appraised. So the HUD proposal would provide more certainty much sooner in the process than what is allowed today under current law because RESPA prevents it from happening.

Chairman NEY. One final question I have and, Mr. Fendly, I do not know if you want to comment on this, but the "Wall Street Journal" ran an article yesterday that stated that all mortgage brokers are making millions off of the refinance boom. And I just wondered if you wanted to give us your——

Mr. FENDLY. I did, Mr. Chairman. I would like to make a couple comments about it.

First of all, the writer picks the top producer at one of the top brokerage firms in the highest cost metropolitan areas in the country to stereotype our industry. And I think it is somewhat absurd to criticize an industry and characterize them in this manner, based on one individual.

But it also states that 5 percent of the brokers make over $1 million, but the average broker made $120,000. Statistically, if you run the numbers, this means the other 95 percent make an average of less than $74,000, working 10 to 12 hours a day, seven days a week—meeting with loan applicants virtually any time day or night.

And I think they have glossed over the good things about mortgage brokers. A wide yield spread premium was used to pay closing costs and consequently, the borrower got a great rate and paid no closing costs. The actual payment for the loan was slightly more than 1 percent—$2,800 on $240,000. And I think this underlines our assertions that yield spread premiums are used to help the borrower. And furthermore, 1 percent on a loan is a far cry from 6 percent realtors make on the purchase of a home.

Now, it is true, some loans are less labor intensive than others, but just like the realtors, some homes sell faster than others, but they still get their 6 percent and that is pretty much non-negotiable.

And last——

Chairman NEY. My time has run out.

[Laughter.]

Mr. FENDLY. All right.

Chairman NEY. Luckily, I think somebody else might want to respond to that, I would assume.

[Laughter.]

Thank you.

Ranking Member—Ms. Waters?

Ms. WATERS. Well, let me apologize for having to go out for a few minutes. Let me pick upon some of the discussion that I heard coming back in. For many years, there have been a lot of questions about fees and charges for mortgage brokers. As was indicated in testimony by our consumer advocate here, the concern about mock displaying all of the charges is a concern that did not just start today, but it has been there for a long time. And I do not have the empirical data, but the reputation of brokers for charging exorbitant fees is a reputation that you have gained, whether or not you are deserving.

If, in fact, there is a belief by consumers, and particularly by consumer advocates, that the charges have been exorbitant, what can you do to convince us who are concerned about that, that we do not need to continue to display every fee that is charged in a transaction?

Let me ask that question of Mr. Courson.

Mr. COURSON. Let me respond from the Mortgage Bankers Association standpoint. Obviously, I think that what you are getting, Congresswoman, is, in fact, the certainty of a one—of a guarantee. The issue today is one, frankly, of an opportunity of bait and switch—of showing a consumer at the time of application a list of charges on a Good Faith Estimate that has no important law to enforce that if by the time that consumer goes to the closing or the funding those numbers change through the addition of fees or other hidden charges and now the consumer is so far down the path they are at the closing table—and under current law, there is no penalty for that.

And so this system is one that says, "Tell the consumer up front, give them a guarantee—a one number guarantee and when they get to closing, that number does not change."

Ms. WATERS. How can I be assured, as a consumer that that one number is not exorbitant? How do I know that you have not doubled what I would have had to pay had I known what the fees for each of the items should have been—could have been?

Mr. COURSON. That is a very good question. If, today, you took a Good Faith Estimate, which you are given, which is a laundry list, if you will, of charges and tried to shop it, I would submit to you that even some of us in the business would have difficulty shopping that to try to match up different fees, different language, different terminology, different charges. And, in fact, very honestly, we talk about predatory lending, if—anything that has that much confusion in it is, in fact, an opportunity to fool the consumer.

So now, what you do is with one number—that is a shopable number. They now have one figure that they can shop with other originators. You know, when a customer comes in to one of our branch offices—consumer—they really, in all due respect, want to know two things—maybe three. One, how much cash do I have to bring to closing? What is it going to cost me? How much cash do I have to have? And what are my payments and my interest rate?

And I will tell you that my experience in 40 years in the business—of people looking at Good Faith Estimates and trying to, if you will, see if the pest inspection or the flood certification or the whatever else we have certifications are marketable—in our market, it just does not happen.

So let us simplify it—give them one price and now they can call any company and say, "I have been told my closing costs for this transaction are not going to exceed X, what are yours?"

Ms. WATERS. But does this make it very difficult for small businesses to be competitive where the big boys just wipe you out by undercutting all those prices that you are getting?

Mr. COURSON. Well, in all due respect, if I thought that, I would not be here testifying as part of this. I do not—I do not envision being wiped out.

[Laughter.]

Actually, I think it proposes some opportunities. We do compete against the big people now. The lenders are out there—they are certainly much better capitalized—lower cost of funds. They have affiliated business arrangements and they compete on closing costs, too. I mean, we are out there trying to originate loans and close loans and competing with rates and fees and closing costs.

Frankly, I think this gives the small business person such as myself an opportunity to come in and form co-ops, affiliations—you read about groups that are forming—which allow us, frankly, to go with others and, perhaps, negotiate better transactions to compete more effectively than we do, really, head-to-head today.

Ms. WATERS. Thank you very much.

Chairman NEY. Thank you.

Mr. Green?

Mr. GREEN. Thank you, Mr. Chairman.

I have a few questions for Mr. Friedlander, if I could.

Mr. Friedlander, the assumption that HUD is apparently making with its proposal is that title companies and other service providers have a fee that is large enough that it needs to be, essentially, attacked or squeezed in the packaging. And then they assume that that savings will be passed on to consumers. What is your reaction to that assumption?

Mr. FRIEDLANDER. This has been one of our major concerns about the packaging proposal. The squeezing of the title service fee is going to hurt the small business. First of all, we have to give quality service and we have to give a quality product. We are highly regulated by the state's departments of insurance. And being able to reduce the price of a insurance policy is absolutely wrong and illegal in Ohio. So we would have to have some preemption, to start with, in order to change the title insurance premium.

To reduce the cost to the point where we will no longer be able to give the quality of service I think would be a detriment to the consumer.

The packaging fee will be a fee and the packager will not disclose what is actually in the package. So we may be reducing our costs, but the package price may just result in additional profit to the packager or to the lender if he is the packager.

Mr. GREEN. Well, I guess the question is if the proposal is—if, in fact, it is going to lower costs to consumers, why should we care if the packaging proposal favors big lenders or big title companies over smaller ones? I mean, why should any of us up here care about that?

Mr. FRIEDLANDER. If it was a matter of reducing costs because of efficiencies, that would be one thing. But it is reducing costs by squeezing the title company. And by squeezing the small agent, it would virtually put them out of business so only the large title companies would be able to compete and the playing field would not be level.

Mr. GREEN. You said something a little earlier that caught my attention. You said that in Ohio—did I understand you to say that there are—that you are state regulated to the point where you do not have flexibility—is it in the rates that you provide or the fees that you charge?

Mr. FRIEDLANDER. There are—there are different ways of charging fees in different states. Some states have what is called a single price that would include the title search, the premium and the closing costs. In Ohio, the premium is the only regulated part of the fee so that the title search and the closing costs are work charges—the title insurance premium is regulated by the state.

Mr. GREEN. And then something else that you said in your statement that I found interesting—you pointed out that in Ohio—I think you said the custom is that title insurance is split half-and-half between the buyer and the seller.

Mr. FRIEDLANDER. Yes, that is correct—in Ohio and in many other states, that the seller and the buyer split the costs of the title—in some places the seller pays all of it. For example, in Cleveland, the conveyance fee tax is generally paid by the seller. In other parts, it is split half-and-half.

Mr. GREEN. So in other words, this proposal is going to have a very different—a varied effect, I should say, state-by-state because of the way that the transaction is treated now under current law.

Mr. FRIEDLANDER. In every state the regulations are a little bit different. Some states are highly regulated. But in all states, the state department of insurance controls the fees of the premium. And I would say that there would be a—really an unfair situation where we would be charging a lower premium to a purchaser who is buying a property being financed by a large lender and charging a different premium by a purchaser who is coming from a smaller lender. I think that would be illegal. In fact, the NAIC—the National Association of Insurance Commissioners—have written a letter that—I will provide a copy of that to the committee.

Mr. GREEN. Thank you.

And just with the brief time I have left, Ms. Saunders, have you had a chance to see the two package proposal that the title companies have talked about? And do you have any reaction to it?

Ms. SAUNDERS. Yes, I have seen it. And I do have a reaction to it. I think that, unfortunately, it would not work. Let me make it clear that we have no problem with anybody offering a package. Our problem is the Section 8 exemption being provided in response to a package. Our concern is that a consumer not be tied into a portion of the closing costs of the loan without knowing what the loan interest rate is, itself.

Mr. GREEN. My time is up.

Chairman NEY. I would note that the time has expired.

Mr. Watt?

Mr. WATT. Thank you, Mr. Chairman.

If I have listened carefully to all of the people on this panel who have testified, I have concluded that the only person who has wholeheartedly endorsed this proposal is Mr. Courson, although the gentleman on the end, whose name I cannot pronounce——

Mr. GARCZYNSKI. Garczynski.

[Laughter.]

Mr. WATT. ——Garczynski—said that he was endorsing it, then he proceeded to say that he wanted several different changes made to it for home builders.

So I take it the only person on this panel who actually endorses this proposal as it is written is Mr. Courson. Am I correct in that?

Mr. COURSON. Congressman, I—let me characterize—I did say in my testimony we have submitted a 60-page comment letter that we did offer some suggested modifications. We certainly support——

Mr. WATT. So you do not endorse it either, then?

[Laughter.]

Mr. COURSON. I did not say that.

Mr. WATT. All right. Well, let me—let me get—I was going to focus more on you because you were the—you were the person who seemed to be endorsing it most. And you seemed to suggest that this will increase competition. And it may well increase competition between lenders. I think some of us are concerned at—about the impact on competition below the level of the lender.

And let me just play this out for you because as I understand this proposal, the Guaranteed Mortgage Package is a one number figure. And if I get a one number figure from you, as a lender, I do not know what is in that one number figure for attorney's fees, for title insurance, for deed preparation, for recording fees. I have got one number. And so I do not find out, as I understand it, until I get to the closing to a settlement sheet what the specific number is for attorney's fees and the various other components of that one number.

How do I, under those circumstances, have the ability to go out and shop, as you said, for a lower attorney's fee, a lower mortgage—title insurance premium? You know, I do not know how—and I think what you said is it might increase competition between lenders, but what you are—what you have done is set up a system where you control the whole system, as the lender, for title insurance, for attorney's fees, for the whole range of other things that are variable. Now, recording fees are controlled. Title insurance premiums may be controlled. But there is a whole range of services that I could go and shop if I had the numbers and if I were inclined to shop.

Now, that is one concern I have about it. And maybe you have an answer to that.

My second concern is that with this Section 8 exemption, which is, in effect, I understand, a safe harbor, if I get down to the closing, I get my fees disclosed—if something is dramatically out of line—suppose you have squeezed everybody—you have squeezed the title insurance company—you have squeezed the title lawyer and, in the process, what you have done is you have increased the amount of fees that are paid to the lender. And now you are telling me I cannot even—I do not even have any recourse against you for doing that because you have got a Section 8 exemption there.

Now, those are the concerns I have about what you are saying. And perhaps there are responses. I hope you will use the balance of the time, maybe, to respond to it.

Mr. COURSON. I would be happy to, Congressman.

When a consumer comes to one of our offices, they want a loan. They want a mortgage loan.

Mr. WATT. No, I want the best loan I can get. I mean, I—and I want the best legal fees I can get. I want the—you know, I want to have the option to choose to use a lawyer friend of mine, even if—even if he charges me more. If you are not telling me how much he is charging for that, I do not—you know, you are assuming the only thing I am looking for is a loan. And that is just not the case in my experience.

Mr. COURSON. May I finish? I will finish the rest of my answer now.

And when that person comes, they obviously are concerned about the amount of cash that it is going to take to close that loan and the rates and the payment that they will have. And I will submit to you today, Congressman, that people that come—the customers that come to one of our retail branch offices—coming for a loan do receive a piece of paper that has itemized costs on it. And——

Mr. WATT. But does—is that required under this?

Mr. COURSON. It—well, no, it——

Mr. WATT. I am saying required under this—under these regulations.

Mr. COURSON. That is correct.

Chairman NEY. I am sorry, the time has expired.

Mr. Shays?

Mr. SHAYS. Mr. Chairman, thank you.

I enter into these questions with some reluctance because I, frankly, think that this is some of the most confusing stuff. I have had about seven closings in three years. I have signed more things. I do not pay any attention, frankly, to what I sign. I hire the best lawyer I can hire to trust him. And I hire a broker—a real—a broker who I can trust and then I just have them give me the one page that summarizes. And then I go back and I figure out when I refinanced if I am paying less each month than I was the last time. And then kind of feel pretty good about it.

But I am saying to you that most of what I fill out I think it is junk—I think it is stupid. And I know that somehow we are responsible for it right here—all of you and all of us.

[Laughter.]

And so, I am just curious as to have someone here, as clearly as possible, without using words like "it will be a disaster," tell me why this is not good to have it be easier and less expensive.

Chairman NEY. Anybody want to offer?

[Laughter.]

Going once——

Mr. FRIEDLANDER. The issue that we are dealing with is a change in a current regulation. We have all agreed——

Mr. SHAYS. Well, my philosophy is that anything that is going to change what currently happens is 50 percent likely to be an improvement.

[Laughter.]

Mr. FRIEDLANDER. The RESPA rules have needed modification and changes. It is very difficult to make these changes. And in order to make the changes, we have a lot of people sitting at the table with a lot of different interests.

Mr. SHAYS. A lot of vested interest—correct.

Mr. FRIEDLANDER. The consumer should be number one in this process, but the disclosures that the consumer needs—and I will speak from the title point of view—that in a refinance situation, the consumers needs are not the same as in a purchase sale transaction. Certainly there is need to know "What am I getting?" And this is part of the problem that we see in this proposal—it is blind. The consumer does not know what is in the package—he does not know if he is getting an appraisal. He does not know if he is getting an owners policy.

And this is why we are——

Mr. SHAYS. But, you know, the sad thing is even when you sign the documents, you do not know.

Mr. FRIEDLANDER. I am sorry?

Mr. SHAYS. Even when you sign all of those documents, you do not know what you are getting.

Mr. FRIEDLANDER. In this proposal——

Mr. SHAYS. No, under present circumstances.

Mr. FRIEDLANDER. You are probably right.

Mr. SHAYS. You are under this assumption that all of these papers tell me something. There is so much and it is—you know, there is only about two pages in the entire document—the summary—that I find valuable. Everything else, I do not find valuable.

Ms. CANFIELD. Perhaps if I could say something, Congressman, I think that is why the lender trade associations do support the rule with some modifications to make it simpler, because the services that are going to be included in the Guaranteed Mortgage Package are not for the benefit of the borrower, really—for the—for the benefit of the lender so that the lender can make the loan. And if the consumer is—if we get Section 8 relief, you will see downward pressure in pricing on all sorts of services that go in that package because packagers, not just lenders, will be able to average cost price.

In addition, from a simplification perspective, the consumer will get that one number at application. Now, what we have also suggested is that the changes in the GSE be postponed so that if the consumer wants to, as under existing law, go choose the title—go choose the closing attorney or a separate title policy or whatever, they can—they can operate under existing law and continue to do that.

But what we are talking about here is allowing for the option for all the settlement services to be guaranteed at application to the consumer.

Mr. SHAYS. The one tragedy in this business, as I see it, is I have a lot of constituents who basically may have missed a month—have kept current, but they are always one month or two months behind. They have not been able to refinance in the last four or five years. The irony is they need these—refinancing more than anyone else, and they are the ones that have the least likelihood of being able to do it. And yet they have been constant in their payment, they just were behind years ago. And I would love to find a way that this committee can solve this problem. And I will tell you, that is one reason why I chose to be on this committee.

Chairman NEY. I thank the gentleman.

Ms. CANFIELD. I will talk to you.

Chairman NEY. A response to that?

Mr. TAYLOR. Very quickly.

Chairman NEY. You were still yellow.

Mr. TAYLOR. I can tell you, as a lender and a local lender and that is our main business, that why this guaranteed package becomes an interesting alternative is nobody looks at those numbers which are itemized. Nobody understands them as a consumer. It is not that they are good or bad or that the good intentions did not bring them to the table. The fact is that nobody knows what they are about, so nobody does look at them.

What the Guaranteed Mortgage Package allows to happen is one number be given to that consumer when they walk in the door because there is two questions that they ask me: What is my rate? And what is it going to cost to close? And that is all they need to know, from their perspective. I am not suggesting that is all they need to know—that is what they think they need to know. And there is nothing else that you are going to tell them other than "Here is my rate, and here is the closing costs in this loan."

When you give them that itemized list, the fact of the matter is, nobody looks at it. They say, "Where do I sign? You tell me." So they are relying on community institutions already to guide them through the process and to tell them what is right and what is wrong and where they should sign.

Chairman NEY. Thank the witness.

Mr. Davis?

Mr. DAVIS. Thank you, Mr. Chairman.

Let us assume for a minute all of the virtues of the Guaranteed Mortgage Agreement in terms of consistency and predictability. As I look at the regulations, one of the things that really strikes me is kind of a catch-all exception that says that the price can be modified, subject to—the language, I believe, is "acceptable final underwriting and property appraisal." Now, we struggle with reasonable doubt in this society. We struggle with preponderance of evidence in the civil cases. That strikes me as being one of the more untrammeled standards I have ever seen, frankly.

Can any of you explain to me why that exception and the reference to "acceptable, final underwriting and property appraisal" does frankly not constitute such a big potential exception that it rips a hole through the whole—virtues of the mortgage agreement?

Yes, ma'am?

Ms. SAUNDERS. I would agree with part of what you said and try to distinguish another part. We have expressed very deep concerns about the meaning of "subject to final underwriting." The idea behind the Guaranteed Mortgage Package, and we support this idea—that the consumer gets to call up four or five different creditors and say, "Here is my Social Security number, here is my income, here is what I think the house is worth. Will you do an initial credit analysis and tell me what I qualify for, assuming that the information that I gave you about the house value and the income and any other questions that I am answering for you are true?"

The black box that we all do not understand of credit worthiness, then, is resolved before the consumer pays anything. And that allows the consumer to shop between lenders about all those issues which most consumers do not understand, which is what loans they actually qualify for.

The issue of how much the house is worth is going to stay the same. It will be resolved by an independent appraiser, regardless of what lender that the consumer eventually chooses.

So the idea is that the consumer will get a commitment on points, and on costs to close and interest rates, subject only to verification of the information that the consumer has the ability to determine himself—him or herself, up front. But HUD has not been clear in the proposed regulations what "final underwriting" means. If it only means determining verification of those things, that is fine. If it means something more, we have concern—great concern.

Mr. DAVIS. Let me follow before anyone else answers—that there is another item in the regulations that do not make a whole lot of sense to me. Given the fact that this particular provision does not require a disclosure of the itemized costs, how would a litigant or how would a potential buyer have a clue what in the world would potentially constitute "underwriting and property appraisal" if all you get is a final number and you have no capacity to actually pull out the itemized costs?

That strikes me as a major tension in the regulations.

Mr. COURSON. Congressman, there is, as part of the proposed disclosure in the HUD rule a disclosure where the lender does disclose certain services whether they—yes or no answer they will or will not obtain, appraisal being one, for example. So they will tell the consumer—there is an addendum says I will or will not get an appraisal. And certainly in most states there are laws on the books that the consumer is entitled to a copy of that appraisal or their credit, if in fact it is—there is one that exists.

Mr. DAVIS. Ms. Saunders?

Ms. SAUNDERS. That is another problem with the rule, frankly. If you get—if the lender gets an exemption from Section 8 for providing the package, then at closing it turns out that the lender has not complied with the promise, all the consumer has is the ability to bring a Section 8 case. But the consumer does not have any of the information, as you have just identified, to enable him to bring the Section 8 case. So losing the exemption means you now have a right, which you have no ability to enforce.

So what we have proposed is that if HUD moves forward with this, they have to say that if you do not keep your promise, you have got—you have created a presumption that Section 8 has been violated, otherwise, taking away and then giving back the Section 8 exemption is meaningless because the consumer would not have the information.

Mr. DAVIS. One final question before my time runs out—given the fact that these cases would be litigated in the state court, I think almost all of you would agree that certain states might have widely varying definitions of what fits this criteria. So, were any of you proposing to possibly federalize this cause of action? And if you are not proposing that, how do you deal with the inherent inconsistency that would result?

My time has expired, but, Mr. Chairman, if you would indulge someone answering that?

Mr. COURSON. Under the two package agreement, our closing package—we do not require a Section 8 exemption.

Ms. SAUNDERS. It is already a federal claim.

Mr. DAVIS. Okay.

Ms. SAUNDERS. So it would be a federal claim.

Mr. DAVIS. Thank you, Mr. Chairman.

Chairman NEY. Thank you, Mr. Davis.

The gentlelady from Florida?

Ms. HARRIS. Thank you, Mr. Chairman.

I came to this meeting today wondering what was good about this package. And I did not like the idea that larger lenders might have the—that we might have been creating an unfair competitive advantage for large lenders over small and other small businesses.

But I cannot help but make the assumption that Secretary Martinez would only be doing this for good reasons. And by listening to you, it sounds as though we are—he is trying to, of course, lower costs and simplify the process.

I think it still comes down—that is really what I want to know—is that going to happen? Are consumers really going to experience lower costs? Or are lenders just going to experience larger profits? Are we really going to create the kind of competition that, in essence, less—it would simplify in that the consumers would bear a smaller share of the cost?

And then on a smaller—on the micro—the second part of the question is—two more questions—why cannot we list out—even though I know that it is complicated and they do not go to look at each of the different—pricing of each service and they each come in for different things, why not be more transparent? Why not list them all out?

And then the second part of that is why cannot the borrower choose if they have an attorney that they feel close to—if they have a relative in the real estate business? Why cannot they opt to choose those individuals or those businesses should those individuals be able to comply with the lenders' specific price points?

Mr. FENDLY. Mr. Chairman, can I answer the last two first? And then——

Ms. HARRIS. Yes.

Mr. FENDLY. I think the issue of listing them out, if you would—remember, this is a guarantee now, that is given at the time of—within three days of application. Today the system—we list them out on a Good Faith Estimate. But, remember, there is no enforcement provision if you are right or wrong or have listed some or not listed some or omitted some or put the wrong price. Now we are putting a guarantee out, so in some respects, frankly, as an originator or lender, we are taking some risk in that we have missed a cost or we have mis-estimated or mis-priced a cost, but yet we are guaranteeing that. So there is a difference between listing them as an estimate that has no enforceability or giving a guarantee as to what those costs will be.

Ms. HARRIS. If you were working with specific vendors, if you will or specific service providers and they had committed to that cost, then at least you would have that backup provision. But if others would also be willing to work for that amount, then it would seem that the transparency aspect would be important, just to be able to show.

Mr. FENDLY. Some may or may not. You know, we focus very different—well, we focus on the package concept here. The basic tenet of the proposed rule is that the customer has a guaranteed settlement fee disclosed to them. The idea of putting together packages, if you will, is sort of an off-shoot of the basic tenet of the rule, which is tell the customer up front and give them a guarantee of what their settlement service costs are going to be.

And so, in many packages that will go forward, there may or may not be discounting or packages, if you will. It may be that the originator knows for that type of loan in their marketplace that the closing costs will be this and they are willing to guarantee that and have to compete because they are going to have to be competitive as that—as that package does get shopped elsewhere.

And if the consumer asks—if any came in and asked for an itemization, there is nothing that precludes an originator or lender from giving him the list of the charges.

Mr. COURSON. If I may, this is exactly what we are talking about in our two package proposal. What the lender needs in order to make the loan is the lender's concern. And that is—they know what they have to do. But the second part of the package, the settlement part, we feel strongly that the consumer has the option to choose what he wants in that package and whether he wants an owner's policy—whether he wants a survey.

These are items that he may choose to get for himself where you have a buyer and a seller. So our proposal simplifies, itemizes and allows choice. Every area is a little bit different—different needs in different places. And I think that the two package proposal certainly would answer that issue.

Ms. CANFIELD. I guess, Congresswoman, I have a slightly different view. RESPA was created over 30 years ago and it was based on the premise that consumers would shop for all these settlement services. Thirty-plus years later, they do not shop for those services.

With regard to itemization, the fact is that in a Guaranteed Mortgage Package there will be some loans where, you know, the lender—or the packager and the lender will not feel it necessary to make a full-blown appraisal. They might be able to do an automated evaluate—automated appraisal. They might decide that a more simplified title insurance arrangement is appropriate for that loan. So borrowers of the services on those loans are going to vary. In addition, the pricing on them will vary.

And as these packages are going to be put together, packagers will go out and negotiate volume discounts and they will say, "Okay, for the first $100,000—100,000 loans, we will give you a price we will set at, say, $100 a loan. If you bring us 500,000 loans, those appraisal prices are going to go down to $50 a loan." So you do not know, for the consumer, which loan is actually getting which price appraisal or which price service.

The idea here is that competition in guaranteeing the consumer a package price—one price up front at application that competition will simply the process for the consumer, drive competition in the cost of those services and ensure that the consumer understands the transaction better than they do today.

Chairman NEY. Time is expired.

Thank you.

The gentlelady from California, Ms. Lee?

Ms. LEE. Thank you, Mr. Chairman.

Let me first say the more I listen, the more questions I have. But I know I only have a few minutes. So let me see if I can move it pretty quickly.

First of all, it seems to me that somehow—and I cannot get my hand on it yet, but it seems like under this Guaranteed Mortgage Package the consumer, the smaller institutions, the smaller law firms—they are going to get the short end of the stick. And I cannot really figure out how they are going to get the short end of the stick, it just sounds like it.

Let me ask you one question with regard to—and I am trying to unravel this—in the bundled package, for example, you lock in an interest rate. Does the consumer know that you pay a point or whatever it is now to lock in this interest rate? Is that disclosed? I believe now under Good Faith Estimate you are required to—if you lock in an interest rate—to say, "Well, you are going to pay a premium for this."

Mr. COURSON. The interest rate component that they receive when they receive a good faith—or a Guaranteed Mortgage Package contains the cost and it contains an interest rate that is based upon or tied to an observable or verifiable index. In other words, some borrowers come in and do not want to lock their loan right away. They want to float with the market. Some of them think they are maybe smarter than we are, so they do not lock their loan right away.

And what this says is if they do not lock, from the time they get the Guaranteed Mortgage Package until the time they lock, their loan—their interest rate they are quoted will not move by more than the market index on which their loan has been based. So they have—in effect, they have avoided the bait-and-switch where you tell them one thing and then the market moves a half-a-point, but you ratchet up the rate a full point. So they have that.

Now, any time they come—and for that—and for the issuance of that Guaranteed Mortgage Package, there are no fees permissible under the proposed rule.

If in—if sometime they come back and they want to lock their loan later, or so—and then, as in today, that is an agreement and whatever, you know, they agree to and the lender charges, it would be an agreement to collect a lock-in fee, but only when they lock in the loan and assure that that is going to be the absolute rate.

Ms. LEE. And the average consumer is supposed to understand this and know this and be able to shop around and call three lenders within three days—and five lenders within three days and make some kind of rational informed decision on which option they would want?

Mr. COURSON. I would suggest that, as opposed to Congressman Shays' stacks of paper and what they go through today, this is a far superior opportunity for the consumer to make sure that they are getting the best deal.

Ms. LEE. Let me ask you, with regard to the subprime lenders—that maybe I can get a clear answer on that—why are—and I—it is my understanding subprime lenders are exempt from the RESPA regulations. Are they—are they required to comply also?

They are? Okay. What about home equity loans? What about reverse mortgages? Are all mortgages—does RESPA cover all mortgages?

Ms. SAUNDERS. Yes.

Ms. LEE. All types of mortgages—subprime?

Ms. SAUNDERS. No. Currently RESPA covers all subprime mortgages, however it does not cover open-end lines of credit.

Ms. LEE. Does not? Okay.

Ms. SAUNDERS. No. The disclosures are not required for open-end lines of credit. So those are—home equity lines, if you—if you mean by that you get a $25,000 line of credit——

Ms. LEE. Yes.

Ms. SAUNDERS. ——and you would be able to draw down $1,000 and pay it back and draw down another $1,000, RESPA does not—is not——

Ms. LEE. It does not cover that.

Ms. SAUNDERS. ——at this point. It could be——

Ms. LEE. Yes.

Ms. SAUNDERS. ——that is a matter of regulation. HUD could decide to cover it and we have, in fact, recommended that HUD do cover home equity loans.

Ms. LEE. Okay. Good because I know senior citizens, oftentimes, take home equity loans and they need, I think, to be covered under this. And—you all have sent in a recommendation on that?

Ms. SAUNDERS. Yes, ma'am.

Ms. LEE. Okay. On the unforeseeable circumstances, can anyone define what "unforeseeable circumstances" means? I mean, what is that? Does anybody have an understanding or can define what that means? I think it is—HUD provide for that, as it relates to a brokers obligation to live up to the terms that any—I think the language in it is "any emergency making it impossible or impractical to perform."

Ms. CANFIELD. Are you referring to the changes on the Good Faith Estimate, Congresswoman?

Ms. LEE. Yes, as it—yes, in terms of how you get out of the loan—that is a clause that—it is sort of an out clause, as I understand it.

Ms. SAUNDERS. Another—may I address that?

Ms. LEE. Yes.

Ms. SAUNDERS. As I said in my testimony, there are three different proposals which HUD is making and they are each substantively different. The third one, which we have spent very little time here discussing, would require that there be very little change that lenders make on the third party charges from what is disclosed on the Good Faith Estimate, which you get three days after application, to what you actually have to pay. We are not talking any longer about the package.

Ms. LEE. Yes.

Ms. SAUNDERS. This is, essentially, the current method ramped up. Right now, if you apply for a mortgage, you will get a good faith estimate a few days later which will say, "Your title insurance will be this much. Your appraisal will be this much. Your—" and so on, but when you—when you go to closing, there is nothing in the current law that requires that mortgage originator to have kept those promises. The disclosures that are made in the Good Faith Estimate are not privately enforceable.

So if, as happens all the time, you—the consumer goes to closing and the charges are considerably higher than promised in the GFE, there is nothing the consumer can do, except to walk away from the loan, which is generally not an option.

Chairman NEY. Time.

Ms. SAUNDERS. So what HUD has proposed is that there be a very small tolerance between what is proposed—what is disclosed up front and what is actually charged at the end. And then HUD said you can get out of that—the originator can change that for unforeseeable circumstances, such as the house is not a house, it is a farm and the appraisal is far more complicated to do than just reviewing a one-story house.

Chairman NEY. The time has expired. Thank you.

The gentleman from Ohio, Tiberi?

Mr. TIBERI. Thank you, Mr. Chairman.

I was a licensed realtor in Ohio and you all have succeeded to confuse me today in your testimony.

Mr. Courson, if you could explain something to me—a comment you made—and let me frame the issue. Mr. Fendly, I believe, said that the proposed rule—the 1 percent cap on FHAs would essentially put brokers out of the FHA business.

Is that correct, Mr. Fendly?

Mr. FENDLY. Correct.

Mr. TIBERI. And you also said that 31 percent of the market right now in FHAs is provided by mortgage brokers?

Mr. FENDLY. Also correct.

Mr. TIBERI. And, Mr. Courson, you said that the proposed rule would increase competition in the lending area. How does 31 percent of the lending going away increase competition?

Mr. COURSON. Our comments also included the fact that there is an inconsistency and have asked—have asked the department to revise the 1 percent cap. There is an inconsistency there. It has been there for a number of years. That regulation has been there for a long time and is inconsistent with the current proposal. And so we have—now, with the guarantee, we have also made the same comment as the National Association of Mortgage Brokers.

Mr. TIBERI. Do you believe that HUD has the ability, Mr. Courson, to raise the cap?

Mr. COURSON. I do not want to speak for what HUD can or cannot do, but it is—and it is—and I am not an attorney, but it is my understanding it is a regulation, so it could be changed by a regulatory proposed rule or regulatory rule.

Mr. TIBERI. Mr. Fendly, do you believe that they have the ability to raise the cap?

Mr. FENDLY. They do—whether they will do it or not remains to be seen.

Mr. TIBERI. Mr. Taylor, do you have the—do you believe they have the ability to raise the cap?

Mr. TAYLOR. We believe—excuse me—yes, we do and we do believe that his regulation could be, in part, brought to fruition through HUD—that there needs to be no further regulatory or legislative action taken.

Mr. TIBERI. Mr. Fendly, why do you believe that the cap causes your members to—how do I want to put this—not be able to make the loan?

Mr. FENDLY. You are referring again to the FHA loan?

Mr. TIBERI. Yes.

Mr. FENDLY. Historically, a broker will receive compensation—two forms on an FHA loan. The direct compensation would be the one point cap on front. The indirect compensation is the yield spread premium, which they will charge, generally speaking, an average of another point, in order to cover their costs.

By recasting that yield spread premium from indirect compensation to direct compensation, that violates the cap that is in current existence right now because that would be two points. It limits us to one point and there is absolutely no way we can cover our costs with one point.

FHA loans, by their very nature, are more difficult and time consuming to consummate than a conforming loan.

Mr. TIBERI. And Mr. Taylor, you would agree with that?

Mr. TAYLOR. Yes, I would—yes, I would.

Mr. TIBERI. And Mr. Courson, you would agree with that, as well?

Mr. COURSON. Yes. The 1 percent cap, Congressman, is years old and it was always assumed that a FHA loan is a 1 percent origination fee—there is an interest rate and there is a discount. And as, obviously, you well know, that marketplace changes and now we are into providing closing costs through grades of trade-off, if you will, of the teeter-totter. And all of that new innovation and new financing tools that are available have really rendered that regulation antiquated and outdated.

Mr. TIBERI. Back to you, Mr. Fendly, you mentioned in your testimony about no-point loans and advertising. Explain to—explain to us a little bit more why you believe that is a disadvantage to brokers, as opposed to others in the lending field.

Mr. FENDLY. There is re-characterized in the yield spread premium, once again, from a direct compensation to direct compensation. As such, a retail mortgage lender and a mortgage broker offer the same loan at the same terms and they are receiving the same amount of indirect compensation. However, in order to advertise that, by this proposed rule, we would have to show that as a one point direct compensation fee—in it—in any——

Mr. TIBERI. A one-point direct compensation fee to—

Mr. FENDLY. To the broker—the retail mortgage lender would show zero points. By definition, we would have to show one point for the exact same loan with the exact same costs and the exact same terms. I think it is reasonable to assume that the average consumer looking at such an advertisement would think that a mortgage broker was more expensive.

Mr. TIBERI. Why are not they, then, in your—in your mind?

Mr. FENDLY. I am sorry?

Mr. TIBERI. Why are not they more expensive, then, in your mind, under that scenario?

Mr. FENDLY. Well, the biggest reason is because we are in the communities themselves—we are actually in with the local people. We work in their communities. we are strengthening home ownership in their communities. we are going out to their homes. We make those house calls. We deal with these borrowers frequently, for years and years and years and subsequently their children. We provide better prices, better service and better product.

Mr. TIBERI. Under the FHA, you said that you—your industry provides 31 percent of the loans. Do you know the breakdown for the rest of the 69 percent?

Mr. FENDLY. I do not.

Mr. TIBERI. All right. Do you provide the largest bulk, do you know?

Mr. FENDLY. I do not know the answer to that question, Congressman.

Mr. TIBERI. Mr. Taylor, do you know?

Mr. TAYLOR. No, I do not have any specific numbers, Congressman.

Mr. TIBERI. Okay.

Mr. Chairman, I know my time has expired. I would just like to submit for the record the Uniform Mortgage Cost Disclosure that was part of the comment period that was provided by the mortgage brokers. it is a disclosure form. I would like to provide it into the record.

[The following information can be found on page 450 in the appendix.]

Chairman NEY. Without objection, provide it for the record.

Thank the gentleman.

The gentlelady from Pennsylvania?

Ms. HART. Well, since Mr. Tiberi was a licensed real estate broker, I was a licensed title agent and an attorney who handled quite a bit of mortgage closings and used to—I will not admit it, but giggle at some of the forms that I had to have people sign.

So when I heard that this was being reviewed—what was required—I was pretty happy about it. But, unfortunately, I have not been completely happy with the result. But listening to all of you today, I guess I am in good company.

My question, actually, has to do—back—and I hate to keep asking questions to create sort of a fuss between the brokers and the—and the mortgage bankers, but I am going to do that.

The RESPA—actual preamble to the change in the—in the reg stated that mortgage brokers originate more than 60 percent of the residential mortgages. And I know it was also cited in some testimony today. That would lead me to believe, since the market usually works—it always works if we let it—but—because it usually works, but if we interfere with it a lot—that would lead me to believe that mortgage brokers provide a product that the public wants.

That having been said, I would like anybody who represents the actual mortgage bankers themselves to tell me, in light of the fact that we have heard that a number of mortgage brokers will be put out of business by this, what are you going to do that is different than what you do now to fill in the blank? What would you have to do differently than you do now to fill in the blank if all of these mortgage brokers are put out of business?

Ms. CANFIELD. I—John, do you want me to take this? Okay.

First, the brokers are a very valuable distribution system for the lenders' loans. And we think that they will—and want them to continue to remain a very valuable distribution system for our product.

With the changes that all of the lender organizations have recommended to HUD, we think that will be a reality.

The other thing is that with regard to the Guaranteed Mortgage Package——

Ms. HART. Before you go on, you are suggesting then that they will not go out of business as a result of this?

Ms. CANFIELD. We certainly hope not.

Ms. HART. Okay. Go on.

Ms. CANFIELD. Secondly, with regard to the Guaranteed Mortgage Package itself, what we see happening is that there will be the manufacturers of the packagers—of the package and then the distributors for the package. So the distributors will be not only lenders and bank branches, et cetera, or mortgage bankers, community—thrift, savings and loans, et cetera, also be mortgage brokers, potentially real estate agents, potentially anybody that wants to get out there and distribute packages to consumers, including title insurance companies. We also think that they will have an opportunity to package—put together the packages.

So I think John mentioned earlier that he thought——

Ms. HART. You think that they will also be, as a result of the package distribution——

Ms. CANFIELD. They will be manufacturing——

Ms. HART. ——originating loans—the mortgage—well, I mean, the only people who can in that category would be the mortgage brokers.

Ms. CANFIELD. Brokers and lenders—you have to be licensed in order to——

Ms. HART. Right.

Ms. CANFIELD. ——originate a loan. So——

Ms. HART. But——

Ms. CANFIELD. ——they will continue to do that. Maybe I am misunderstanding what——

Ms. HART. You are convinced that they will be.

Okay. Let us go back to the mortgage brokers, then. In light of that statement, can you tell me, aside from the issue—or is the main issue the low value—the low amount mortgages and the ones that are government insured that you are not going to make any money on so you are not going to bother with them anymore—is that the issue? Or is there another issue that we are missing that Ms. Canfield has missed?

Mr. FENDLY. I believe there are multiple issues. And certainly the FHA-VA loan program is part of that issue. But to get back to small business again, I think it is very, very important to understand, as the statement you made, my company has five employees. I have been in the business industry for 20 years. You are never going to convince me that I can compete in a packaging scenario with a mega-lender. And quite frankly, our industry is composed mostly of small brokers.

Contrary to what I have heard at this hearing, I believe the only opportunity it provides for small mortgage brokers is to seek a new career.

Mr. COURSON. Can I respond, Congresswoman? I am sorry.

Ms. HART. Well, sure.

Mr. COURSON. Well, you know, one of the—and that is one of the reasons that in our comment letter to the department, we, frankly, have encouraged them—there are two different proposals, if you would, one talking about the Guaranteed Mortgage Package, the other about the Good Faith with the tolerances.

We are saying to the department, "Let us take the package—let us put it into play—let us see if the consumer, the originators, the lenders will accept it." Is the guarantee something that is acceptable in the marketplace? Is it good for the consumer? Is it good for the industry? Does the packaging benefits benefit closure? Because if they do, in a free marketplace it will get acceptance, it will get traction and it will move forward. But do not change both at the same time. Leave the current Good Faith, allow the marketplace to work the way it is working today because if the package, in fact, is viable, then in the—in the marketplace, it will gather that acceptance. And do not change both at the same time.

Chairman NEY. Thank you.

Time has expired.

Ms. HART. Thank you, Mr. Chairman.

Chairman NEY. I want to thank the panel for their testimony—a very interesting testimony on an important subject today. I want to thank you.

Also note—the chair would note that some members may have additional questions for this panel which they may wish to submit in writing to the panel. Without objection, the hearing record will remain open for 30 days for members to submit written questions to these witnesses and to place their responses in the record.

I want to thank you.

We can move on to the second panel, please.

I want to thank the second panel for being here.

The first witness is Peter Birnbaum. Mr. Birnbaum is the President and Chief Executive Officer of Attorneys' Title Guaranty Fund, Incorporated, which is headquartered in Champaign and downtown Chicago, Illinois. Attorneys' Title Guarantee Fund provides title insurance to home buyers and lenders through its network of 3,500 member lawyers.

Dr. Charles J. Mendoza—Dr. Mendoza is a member of the board of the American Association of Retired Persons—AARP. As a former criminal defense attorney, Dr. Mendoza is active in AARP's telemarketing fraud campaign. He has written numerous articles on consumer fraud which have been published in national magazines. He also plays a key role in working with AARP's Hispanic membership. AARP is a non-profit, of course, non-partisan membership organization for people aged 50 and over.

I will see you in a year.

AARP provides information and resources, advocates on legislative, consumer and legal issues, assists members to serve their communities and offers a wide range of unique benefits, special products and services for its members.

Arne M. Rovick—Arne M. Rovick is Vice Chairman General Counsel for Edina Realty Home Services, a large regional broker operating in Minnesota and Western Wisconsin. Edina Realty has had an affiliated mortgage company and an affiliated title insurance and closing services company and an insurance agency that was added.

Arne has been a Director of the Real Estate Services Provider Counsel, Incorporated—RESPRO—and is a past chairman.

Ira Rheingold—Mr. Rheingold is the Executive Director and General Counsel of the National Association of Consumer Advocates—NACA. And NACA is a nationwide association of more than 800 attorneys and consumer advocates who have a wide range of experience curbing abuse of the predatory business practices and promoting justice for consumers.

I want to welcome everyone here today on the panel. Thank you for attending.

And we will start with Mr. Birnbaum.

STATEMENT OF PETER J. BIRNBAUM, PRESIDENT, ATTORNEYS' TITLE GUARANTY FUND, CHAMPAIGN, IL, ON BEHALF OF NATIONAL ASSOCIATION OF BAR RELATED TITLE INSURERS

Mr. BIRNBAUM. Mr. Chairman, thank you.

Members of the committee, I represent a constituency of about 20,000 law firms nationwide that represent the typical mom and pop in their home closing. So I could certainly relate to many of the comments by Congressman Manzullo, Congresswoman Hart, Congressman Watt, Congressman Davis in terms of what it is like to practice law in this area.

We are opposed to the packaging aspects of the proposed rule. And I thought in articulating that we would look back and then look to where we are today before making comments.

When Congress enacted this legislation in 1974, it is clear that it wanted to accomplish four things—one is to give consumers better protection for the largest financial transaction of their lives; two, to prohibit kickbacks because Congress found that the cost of the kickbacks passed on to the consumer; three, to disclose the cost of home sales and home purchasers to the seller and buyer; and finally, to give consumers the right to shop.

RESPA is not perfect, and we heard a lot of comments related to that today. It needs a lot of work—lots of dumb stuff—these closings with hundreds of documents. I agree it is totally confusing. But the concept works. And certainly the proposal does not address some of those comments that were addressed today.

I think it is important to step back for a second and do look at the fact that the closing business and the title business is a highly competitive business. There are lots of competitors, lots of price competition, lots of service competition.

The proposed rule, in my opinion, is going to overturn an important cornerstone in terms of consumer protection in the housing industry. We have got four serious problems with the proposed rule.

First, and foremost, we believe that the proposed rule has the effect, and I think it has been noted by members of the committee today, of eliminating competition and, in effect, giving a monopoly to big banks and mortgage banks. Effectively, small law firms, small title agents are going to be out of business if this becomes a reality.

Second, and startling to me—and I am surprised there has not been more comment on this—is that it gives banks, and no one else, pretty much safe harbor immunity from criminal and civil prosecution for taking kickbacks. One, I question the statutory authority for that and two, when Congress found the need to make this prohibition was specifically to protect the consumer.

Three, it allows lenders to sell these closing services as part of a package with no disclosure to the consumer of what they are buying, from whom or what price.

And then finally, and it was addressed by one of the committee members earlier, it seeks to set a national framework for real estate transactions. And as a result—and I think Congressman Green raised this—it is going to have the practical effect of preempting state law. Before we do that—before we go down that path, we have got to remember that closings are very parochial in nature—who does closings—who pays for these closings—how the services are allocated between the parties in terms of costs—very parochial—a patchwork quilt, if you will. it has always been regulated at the state level and it is impractical, improper and probably exceeds HUD's authority to suggest otherwise.

My opinion if this rule passes—I think that four things are going to happen. One, prices are going to rise. Kickbacks—there is no question in my mind—are going to be passed on to the consumer in the form of higher prices. Also, in terms of cost allocation in seller-pay states, those costs are going to be shifted to the buyer and it is going to make prices rise.

Two, consumers, if they are bewildered today, they are going to be even more bewildered by this process that hides virtually all the costs.

Three, competition is going to be eliminated.

And then, four, all lawyers and all the other small folks that are in there providing this kind of competition are going to be gone from this business.

What do we think you should do? A couple of suggestions—one, there is a lot of talent in this room today, alone. And there is a lot of talent in this industry. And to my knowledge, HUD has not worked with an advisory council on trying—there is a lot of disagreement about how to implement these rules. And I would love to see HUD bring us in to try to work through some of the issues.

Two, I think you should study the costs. The Secretary says that this is going to lower consumer prices. I do not see that. I do not see that at all and I think we owe it to the consumers to study that issue.

Three, I think that absolutely this should be done by legislative process and not by rule. I do not believe that HUD has the authority to promulgate this regulation.

We ask that you not implement the rule as drafted. We think that costs are going to skyrocket. We think that housing is going to become less affordable. There is going to be no less paperwork involved. And a complex process is going to become even more mystifying to the consumer.

Thank you.

[The prepared statement of Peter J. Birnbaum can be found on page 63 in the appendix.]

Chairman NEY. The time has expired. Thank you.

I also would note, without objection, your written statements for the entire panel will be made a part of the record. You will be each, of course, recognized for your five minutes, but it can be made part of the record without objection.

Dr. Mendoza?

STATEMENT OF CHARLES J. MENDOZA, MEMBER, BOARD OF DIRECTORS, AMERICAN ASSOCIATION OF RETIRED PERSONS, WASHINGTON, DC

Mr. MENDOZA. Good afternoon, Chairman Ney and Ranking Members Waters and Members of the Subcommittee on Housing and Community Opportunity.

I am Charlie Mendoza and I am a member of AARP's board of directors. And I really appreciate this opportunity to offer AARP's assessment of the U.S. Department of Housing and Urban Development's proposal to reform the Real Estate Settlement Procedures Act.

We believe, at AARP, that there is a clear need to simplify and improve the process of shopping for and obtaining home mortgages. And AARP strongly supports the thrust of HUD's approach for reforming today's confusing settlement process.

For nearly a decade, AARP has been actively advocating for the reform of RESPA, with these same objectives in mind. Many homebuyers are mid-life Americans buying a long awaited first home, or those who are trading up, or older

Americans who are restructuring their households as they approach their retirement years. Unfortunately, the existing

RESPA disclosure requirements have turned a virtue into a vice by inhibiting, rather than facilitating, competition for loan products and comparative shopping by homebuyers.

Chairman Ney, because of the importance and complexity of the issues being raised, I have attached to my statement a copy of AARP's detailed agency comments regarding the proposed RESPA reform rule. If space permits, I would like to request that our comment letter be made a part of today's hearing record.

[The following information can be found on page 336 in the appendix.]

Chairman NEY. Without objection.

Mr. MENDOZA. Thank you.

HUD's proposal contains three major provisions—enhanced disclosures of mortgage broker or loan originator compensation; revisions to the Good Faith Estimate system, often referred to as GFE

Disclosure; and the availability of guaranteed mortgage packages that include guaranteed settlement costs and interest rates. This loan package is often referred to as the GMP option.

In the limited time that I have to address the subcommittee, I would like to suggest or highlight several key features of AARP's comment letter as they refer to these provisions.

First, AARP supports HUD's proposal to streamline and improve the Good Faith Estimate and to create a new disclosure form to permit the offering of a Guaranteed Mortgage Package. The GMP package carries with it guaranteed loan terms and settlement costs.

Second, we support HUD's proposal to streamline and improve the accuracy of the GFE option. The proposed changes will offer significant advantages to borrowers over the current system by creating greater certainty. The revised GFE will be especially beneficial for subprime borrowers who will receive firmer cost information without the risk of losing important consumer protection rights.

Third, we favor the GMP as a novel concept to promote true comparison shopping by providing certainty for consumers at an early shopping stage.

Fourth, we strongly recommend, however, limiting the GMP package to the competitive prime market until knowledge regarding subprime market behavior becomes more standardized and reliable. Our concern is that the subprime market has not yet developed the required market information that is necessary for creating competitive pricing standards.

Fifth, in our comments to the department, we detail the need for greater enforcement mechanisms for the GFE and the GMP.

And lastly, we suggest revising the proposed GFE and GMP disclosure forms to improve their clarity and comprehensibility.

Arcane as the language of RESPA may be, the substance of RESPA is tied directly to a central component of the American dream, the expectation that most of us, as Americans, will be able to afford to own our home.

We really appreciate the purpose served by this hearing in focusing public attention on an important rule-making proposal and process. And let me close by saying that while a number of important and useful modifications can and should be made to the proposed RESPA rule before final promulgation by HUD, we strongly support the department's efforts to move this rule forward. And we, at AARP, would be happy to answer any questions that you have regarding our proposal.

Thank you.

[The prepared statement of Charles J. Mendoza can be found on page 329 in the appendix.]

Chairman NEY. I would thank the witness for his testimony.

Mr. Rovick?

STATEMENT OF ARNE ROVICK, VICE-CHAIR AND GENERAL COUNSEL, EDINA REALTY HOME SERVICES, EDINA, MN, ON BEHALF OF THE REAL ESTATE PROVIDERS' COUNCIL, INC., (RESPRO)

Mr. ROVICK. Mr. Chairman, good afternoon.

My name is Arne Rovick and I am Vice Chairman and General Counsel of Edina Realty Home Services, a full service real estate brokerage company headquartered in Edina, Minnesota. Edina Realty Home Services is the parent company of Edina Realty, which participated in over 33,000 residential real estate transactions in the year 2002 in Minnesota and Western Wisconsin. Edina is also the joint venture partner in Edina Realty Mortgage, which originated over 6,300 residential mortgages; and the parent Edina Realty Title, which issued over 16,000 title policies and performed 20,000 closings during the same period.

Today, I represent the Real Estate Services Providers Council, known by the acronym RESPRO, of which I have served as past chairman and currently serve as a member of the board of directors. RESPRO is a national non-profit trade association of approximately 220 companies from a cross-section of the home buying and financing industry, including real estate brokerage companies, mortgage companies, title and other settlement service providers.

Mr. Chairman, RESPRO supports the goals of providing consumers early, simple and firm information about their mortgage costs. However, RESPRO believes that HUD's proposed single-package approach to RESPA reform would not accomplish these goals.

First, HUD's single-package approach contains a 30-day interest rate guarantee requirement that will prevent virtually all mortgage lenders from guaranteeing a loan package. This is explained further in my written testimony.

Second, even if it was possible for mortgage lenders to guarantee the interest rate, HUD's single-package approach, as a practical matter, would bar non-lenders such as title underwriters and agents, vender management companies and other settlement service providers from competing with lenders in the packaging marketplace because they do not offer, and therefore could not guarantee, the interest rate or the loan origination services that HUD requires to be included in the package. Instead, they would be forced to partner rather than compete with a mortgage lender if they want to offer a guaranteed settlement service package.

And as a result, we believe the competition that is supposed to pass on cost savings to consumers will be diminished and not promoted.

Let me give you an example from the perspective of Edina Realty Home Services. Our title company currently issues title policies and performs closings on behalf of our mortgage company and over 100 other mortgage originators operating in our marketplace. Edina Realty Title would like to offer guaranteed settlement service packages directly to our real estate customers that could be used not only for mortgages provided by our company, but by any of the more than 100 mortgage originators in our marketplace.

Not only would this allow us to offer more of our real estate customers the potential benefits of packaging, but it would also provide small local mortgage originators in our marketplace a means to compete against the large national lenders.

HUD's proposal, however, would prevent us from offering these packages for these local mortgage originators because we would not guarantee the interest rate and points, even though we could and would offer superior service and pricing with respect to all of the services needed to close a transaction.

Edina is not alone in their willingness to compete and do packaging in the marketplace. A significant number of the nation's residential real estate brokerage companies and home builders offer title services to their customers through wholly owned subsidiaries with joint ventures.

In addition, many title and vendor management companies would like to be able to offer settlement service packages directly to customers that could be used with the loan they eventually select. By excluding such a substantial base of potential competitors from the packaging marketplace, HUD's single-package proposal would effectively put control over the distribution and marketing of settlement service packages in the hands of mortgage lenders. We believe this would diminish competition and will increase prices of loan packages over what they would be in a more competitive environment.

To correct these deficiencies, RESPRO has proposed to HUD a two package concept. Under our proposal, a consumer would shop among mortgage lenders for a loan with a guaranteed price for lender services and among both lenders and non-lenders for a guaranteed price for the closing services needed to close the loan.

Finally, RESPRO believes that the proposed binding Good Faith Estimate—the alternative to packaging—would significantly disrupt the marketplace by increasing liability risks for lenders, creating consumer confusion and increasing administrative burdens for providers in all industries.

In the opening statement of its proposed RESPA rule, HUD stated, "The American mortgage finance system is justifiably the envy of the world. It has offered unparalleled financing opportunities under virtually all economic conditions to a very wide range of borrowers that, in no small part, have led to the highest home ownership rate in the nation's history. Clearly, our residential mortgage industry is not broken. It has functioned well. The residential real estate industry has been one of the strongest sectors of our nation's economy for the past three years. This is not to say it cannot be improved."

We welcome the opportunity to——

Chairman NEY. Mr. Rovick, if you could summarize your testimony.

Mr. ROVICK. Yes. We welcome the opportunity to test the theories of the packaging system and believe that the GFE system should stay in place until the theories of that packaging system are tested in the marketplace.

Thank you.

[The prepared statement of Arne Rovick can be found on page 381 in the appendix.]

Chairman NEY. Thank you, Mr. Rovick.

Mr. Rheingold?

STATEMENT OF IRA RHEINGOLD, EXECUTIVE DIRECTOR, NATIONAL ASSOCIATION OF CONSUMER ADVOCATES, WASHINGTON, DC

Mr. RHEINGOLD. Thank you, Mr. Chairman, and members of the committee for inviting us to testify today.

As I hear people comment about being involved in the real estate process and being involved in the closing process, I also am an attorney who has been involved in the real estate process, although my background is a little different. I spent the last six years, prior to coming to Washington, working in Chicago running a foreclosure prevention project, representing seniors and low-income people in the poorest communities of Chicago who were victimized by bad loans and were facing foreclosures.

So the perspective that I bring and the membership that I—that—of National Association of Consumer Advocates are from people who are representing folks who have been damaged by the mortgage lending process. And the eye we bring toward HUD reforms is that eye. And we look toward it to see whether it is going to help those consumers, as well as other consumers who are confused by the real estate mortgage process.

When we look at the HUD proposal, we have three positive comments. We think that its intention is extremely good. We particularly like the part of the Guaranteed Mortgage Package, which provides an interest rate and closing cost guarantee when a Guaranteed Mortgage Package agreement is offered. The mortgage—the interest rate and closing cost guarantee is essential to help in the shopping process. A package that does not include both closing costs and interest rates would be meaningless because a closing—interest rates can be changed to maximize the benefit for people—to maximize lending industry—I am sorry, let me start again.

If the closing costs are brought down to get somebody to buy that loan, that cost will be made up in the interest rates. We think that unless the package includes both the closing cost guarantee and an interest rate guarantee, the—it simply cannot work.

A second point of the proposal, which is very important and very good is HUD's attempt to re-characterize yield spread premiums as a payment from the lender to the borrower. During the last several years, no issue has been more contentious than the use of the yield spread premiums in the home mortgage lending process. Time and again, consumers have unknowingly received a mortgage with a higher interest rate than they had otherwise qualified for because of inappropriate and illegal kickbacks paid by lenders to brokers in the form of yield spread premiums.

HUD's proposal to change the way yield spread premiums are disclosed is an important first step in allowing consumers to have greater control in choosing the type and structure of their loans and the methods—and in the methods they choose to compensate their mortgage broker.

Finally, in terms of the proposal, we like HUD's bright line rule that attempts to make the Good Faith Estimate a meaningful binding document that provides real information to consumers. it is a game right now and I—as some of the great works of fiction, as clients walked into my office with the original Good Faith Estimate, as I compared that to their closing document. There was no correlation—there was no reality in what we looked at from the beginning of the process to the end of the process.

Making that binding becomes very important for a consumer so that at the end game, when they are trying to close, they are not surprised by costs that have just changed enormously. I think that is an extremely important proposal and a very good thing that HUD has done.

With that as background, we do have some problems with it—with the HUD's proposed rules.

The major problem—maybe not a problem, but a major concern is we think that their proposal does nothing about predatory lending. And if it is not looked at carefully, can, in fact, enable predatory lending.

One of the assumptions that the proposal creates is that people shop for loans. And I think in the prime marketplace, you and I—members of this committee—people here—we may shop. In the subprime marketplace, people are not shopping.

Creating a Guaranteed Mortgage Package with the assumption that people are going to just take that information in poor communities and unsophisticated communities are going to take that information and shop is simply false. And it does not help them. And, in fact, it will hurt them because it eliminates the single biggest tool people will have to defend themselves in foreclosure, which is Truth in Lending defenses. They will be unable—people will be unable to determine whether or not the loan they have violates Truth in Lending with the Guaranteed Mortgage Package as it is currently structured.

And it is crucial that HUD, if they go forward on this, talk with the Federal Reserve—coordinate with the Federal Reserve to determine how those costs function along with Truth in Lending.

I am about out of time, so I am going to stop here. I have additional remarks in my written commentary.

I think overall, the direction that HUD is taking in this proposal is a good one. I think there are specific concerns that we have that they need to amend the proposal so that it really does help people and it does not do anything to extend the predatory lending problem that we see in the country today.

[The prepared statement of Ira Rheingold can be found on page 375 in the appendix.]

Chairman NEY. Thank you for your testimony.

Questions—Mr. Rovick, you talk about a two-package proposal—have you seen the two-package proposal being put forward by the title industry?

Mr. ROVICK. Yes, I have—yes, I have.

Chairman NEY. How does it compare?

Mr. ROVICK. Our proposal differs on two points—one, our proposal does not call for the guaranteed interest rate in the lenders' package for the reasons that the lenders have said—that it is difficult to lock an interest rate for 30 days.

And the second point escapes me at the moment. I am sorry.

Chairman NEY. You can get back to me on it.

Mr. ROVICK. Yes.

Chairman NEY. Mr. Birnbaum, would the two-package proposal—first, have you seen the two-package proposal put forward by the title industry?

Mr. BIRNBAUM. I have.

Chairman NEY. And does that address some of the concerns that you have raised?

Mr. BIRNBAUM. Not completely, but we are talking with ALTA about that issue right now.

Chairman NEY. So you at least see some selling points—some positive effects that you are looking at?

Mr. BIRNBAUM. I do. I am still concerned about who is in control of the process in either package approach. It seems to me that when we look at the packages, a lot of independence is lost in terms of who is choosing and whether the consumer really has a say in that process.

Having said that, though, I have been working with the ALTA folks and they—we are hoping to come up with a agreement.

Chairman NEY. Mr. Mendoza or Mr. Rheingold, I do not know if you have opinions on the two-package proposal?

Mr. RHEINGOLD. I received it this afternoon, so I—

Chairman NEY. Fair enough. Obviously, you can supply comments at a later date.

Mr. ROVICK. Congressman, Mr. Ney, the second point I wanted to make is that in our two-package proposal, RESPRO provides for a Section 8 exemption in the settlement services package, which the ALTA package did not. And we believe that is important so that the vendors participating in that package can freely negotiate the prices among themselves.

Chairman NEY. Okay. Thank you, that is helpful.

One question I had, I guess, for all of you, if you can comment on it. we have had different people, Mr. Birnbaum, for example, make reference to the inconsistencies in some ways of this proposal with some of the state laws. Do you have suggestions on how we might be able to have some sort of reconciliation of these state inconsistencies with the federal proposal?

Mr. Birnbaum, I will begin with you.

Mr. BIRNBAUM. Well, you could start with the—one of the things, I guess, that troubles me the most is this whole Section 8 issue. You know, what we are talking about—it is unprecedented, really, in my experience to allow immunity from prosecution to a class of people while still leaving the rest of the industry exposed to prosecution. And I question whether HUD has the authority to do that independently of Congress. It certainly seems like that would be your province.

If there is a feeling that you want to delegate that back, I suppose being admittedly somewhat myopic on it, if you were to give—leave that up to the states to make that decision—that is something, if I had to live with it, I probably could live with it.

Chairman NEY. How about some of the other inconsistencies?

Mr. BIRNBAUM. Well, again, you know, the packaging idea seems to gut all of the—I am from Chicago and—Illinois, it would seem to be inconsistent with our consumer fraud act. So, again, if you allow the states—and, again, you know, Carl Sandburg called my town the patchwork quilt of cultures. And that is—I think you heard that today in terms of this industry. If you—if you leave it up to the states to govern these kinds of issues—and if HUD wants to make broad policy statements about this, fine. But ultimately, in the trenches, doing—and 90 percent of what we do are mom and pop's bungalow on the north side of Chicago—let our marketplace decide and let our state decide. And that certainly seems consistent with the approach that Congress has taken on this issue.

Chairman NEY. Well, if other members—Mr. Rheingold?

Mr. RHEINGOLD. There is one other matter—one inconsistency and area that I have addressed in my written comments, but I think it is very important that HUD stay out of—in the Good Faith Estimate proposal, there is language in it that I think is extremely dangerous and really would offend state law. And the language gives mortgage brokers a tremendous benefit that we think is extremely dangerous. And I will read a little bit. "We do not offer loans from all funding sources and we cannot guarantee the lowest price or the best terms available in the market."

This is a written document—you have heard all this testimony about people who read that—who do not read any of the documents, yet one of the HUD forms that people are going to be handed is a document that basically says, "I am your mortgage broker, but I am not going to get the best loan for you or I am not going to be obligated to get the best loan for you."

Well, that is fine, except for the fact that in a lot of mortgage transactions, particularly with mortgage brokers, they are telling people, orally, "I am going to get you the best loan. I am going to get you the best deal." And I think it is really dangerous. And there are lots of state law out there that defines when a fiduciary exists and protects people when, in fact, they have been misled or have been told that there is a relationship there that somebody is—a relationship of trust. And I think that language in that federal statute is extremely dangerous. And we deserve some important state protections for the consumers.

Chairman NEY. Thank you.

Thanks to all of you.

Ms. Waters—questions?

Ms. WATERS. Well, I think a lot of my concerns have been addressed. But I guess I want to ask anyone who would like to respond on the panel whether or not you believe HUD has the authority to propose the reforms that are being proposed. I hear a lot about—several people saying they do—they do not.

If you do not believe that they have the authority, tell me why.

Mr. ROVICK. Congresswoman, we believe that there is very questionable authority on the ability to provide for the firm GFE. The legislative history of the statute shows that the prior provision that called for a firm GFE was repealed and in its place the Good Faith Estimate as we know it today was put in there. So we think that the GFE that they have proposed here would not be sustained by the courts. And that is why we have recommended that the GFE program stay in place while we test the packaging.

The packaging issue, I think, is a close call. There are arguments either way as to whether that is supported by the statute or not. And I am not sure which way a court would come out on that decision.

Mr. BIRNBAUM. Congresswoman?

Ms. WATERS. Yes?

Mr. BIRNBAUM. When you enacted RESPA in 1974, I think the direction from Congress to HUD was to implement regulations that were supportive of the goals that were articulated by Congress. Now, by regulation—I mean, frankly, in my market, one of the most important provisions is this anti-kickback provision—Section 8 of RESPA. It keeps people aware—on their toes—keeps the marketplace in check and I think it keeps costs down.

How a federal agency can now, by regulation, grant immunity to a certain class of parties from criminal prosecution is beyond me.

The other issue is state preemption. I think that the policy statement was clear when the statute was enacted as that to the extent that the states offered greater consumer protection that the state statute would control. Here, the packaging proposal, at least my opinion and the way that I think our legislature would look at it, would say that this is taking away important consumer protection, particularly in this area of disclosure and who is paying what for—at what price and from whom.

You know, rather than this being transparent, which is the goal, I would suggest that the closing services part—the pricing is totally invisible to the consumer. And I think that is up for the states to decide.

Ms. WATERS. So you think that any local statues—state or city statues—that create disclosure in a particular way would be preempted—could be preempted if, in fact, we adopted the——

Mr. BIRNBAUM. That is absolutely the way I read this. And that terrifies me. I just do not think it is appropriate.

Ms. WATERS. Any other opinions on authority or preemption?

Mr. RHEINGOLD. I actually do not know the answer to that because, in fact, the way the courts—I did not think HUD had the authority to issue its 2001 letter, which damaged consumers incredibly when they redefined how yield spread premium should be utilized. Yet, courts had deferred to HUD in what they have done. So I am not sure I have an answer to that.

I think that there are much bigger preemption issues that is face—that Congress is facing besides RESPA right now. I think you have a national—you have OCC doing preemption of state laws and city laws. you have got OTS doing preemption. I am not sure that that—this is as big a concern as what we have got elsewhere involving mortgage lending.

Ms. WATERS. Yield back.

Chairman NEY. I thank the ranking member.

The question I wanted to ask you was asked of the last panel by the gentlelady from Florida, Katherine Harris, will this make things better for the consumer in the mortgage market?

Mr. ROVICK. We support the premise underlying the concept of packaging. The one price, all-encompassing package may make it easier for the consumers to comparison shop. But what we disagree with is the single-package approach. But we think giving the consumer a single price for each of our proposed two packages and giving them the ability to compare that with other packages could, conceivably, result in competition.

Chairman NEY. Okay. On that point, just to narrow it down a little bit, then, overall, when you weigh them, what you have said, is the answer no or is the answer yes?

Mr. ROVICK. Packaging has never been tested in the marketplace and, therefore, we would like to see it tested in the marketplace and prove itself out, leaving the current GFE in place as an alternative until the theories of packaging are proved out. But I think packaging may lead to easier comparison shopping.

Mr. BIRNBAUM. Come on, you know, how can it be? I mean, if you have fewer competitors and you have got a scheme where the folks, which are mainly going to be large institutions can control the payments that are flowing to them, which are really, today, are a federal crime—it can be prosecuted for giving and receiving kickbacks.

If they are controlling that process and they are receiving that dough, that money is not going to, you know, be passed on to the consumer, it is going to come in the form of higher prices. So if you have fewer competitors and higher prices, how does the consumer win?

Mr. RHEINGOLD. I guess I would disagree with my fellow Chicagoan a little bit here. I think there is a finite class of consumers who can be benefited by this proposal. I think the GMP works for sophisticated consumers who will understand how to shop around. I think it does absolutely nothing and may do damage to people in the subprime market who are sold to and who are not shopped to.

I also think that there is something that seems to be missing here—is that there is nothing in this HUD package that—HUD proposal that requires lenders to use the GMP. it is simply an option if they are seeking Section 8 exemption.

The GFE will still be alive and well and people can make loans under that—on that criteria, as well. So I think it simply opens another opportunity for lenders to offer a different lending package to people.

So I think that, if done right, I think it will help consumers, even—particularly sophisticated consumers in the prime marketplace.

Chairman NEY. AARP have any pains, Doctor?

Mr. MENDOZA. Well, I am an unlicensed consumer. We can talk about sophisticated consumers but, obviously, I am not one of them.

I think what we need is for the language to be a lot simpler. I looked at one thing there and it said, “Origination charges.” And as I looked, I am thinking—“What are we talking about?” We are talking about what we are going to be charged by the broker and by the lender. I think that—and we put it in our package, as I looked at it, some things that I think we really need to do to make it simpler for the consumer to understand what they are looking at so then they can go ahead and make comparisons. But until the consumer can look at the sheet and understand it, I think we are repeating history all over again. And I am not an expert in this area, obviously.

Chairman NEY. I will yield to the gentlelady.

Ms. WATERS. Let me be clear—as I remember your testimony, you supported this proposed reform for the GMP in offering one price, without having to delineate all of these charges. Is that correct?

Mr. MENDOZA. Yes, because I think that in there is another option. What we are also saying is that you have got to make this cover sheet a lot simpler so the person can understand when they start doing their comparison shopping what it is we are comparing—what price is this versus what——

Ms. WATERS. ——comparing two things now under this reform.

Mr. MENDOZA. Right.

Ms. WATERS. And that is the bottom line consolidated price of all those fees that you used to see that you will not see any more and the interest rate. Is that right?

Mr. MENDOZA. Yes.

Ms. WATERS. So do you think that is simplifying it? Or do you think that is hiding or confusing?

Mr. MENDOZA. Well, we think that this form here simplifies it much more than it is—I was just handed this form here. And we have made some suggestions to this form. We think the form is a good start and you can see in our package, once you get it, that we have added some suggestions, I think, that will make this form a little better for the consumer.

Ms. WATERS. And let me be clear about what Mr. Rheingold is saying.

Are you saying the same thing—that you think that this proposed——

Mr. RHEINGOLD. I think it is a good idea. I think that the concept is a very good one. I think it simplifies the process. I think there are a lot of risks involved in it and I think it has to be done well. I think that when you do the GMP and you give Section 8 exemption that you need to be very—and that is basically an exemption from liability—you need to be very clear about what happens when that gets violated.

I think it can benefit consumers. I think it would make shopping easier for consumers, yes, I do, but I think there are things in that proposal that need to be put in place so that when a lender does not follow the rules that lay—are laid out under the HUD proposal, there is enforcement mechanisms to make them comply. And that is something that is in my written proposal, but I think it is also—it is very important to make it work.

Ms. WATERS. Okay. Just to make sure that I am understanding you correctly—you believe that there are things that can be done to make the proposal beneficial to the consumers without identifying all of the fees and charges?

Mr. RHEINGOLD. Absolutely. I mean, I have to tell you, I have gone over more closing documents with consumers who were faced with foreclosure who had no clue as to what all of those charges were. Simplifying the process, saying, "Here is your closing costs, here is your interest rate," would eliminate a lot of confusion. I think that is a good idea in concept—yes, I do.

Ms. WATERS. Thank you.

Mr. ROVICK. Congressman, I would just like to amplify—the complaint in today's market is that there is 30 to 40 itemized items on a HUD one settlement sheet. So I think by having two packages with two prices simplifies all of those line items.

We disagree with HUD—we do believe that the services which are provided within each of RESPRO's proposed two packages should be itemized so the consumer knows what services are being provided. But we think that there is some merit to the single price on each of the two packages in enabling the consumer to comparison shop with other providers.

Ms. WATERS. So you think—what you are telling me is you think you should list out lawyer's fees, pest control fees, et cetera, without putting a price beside each of them and just say, "These are the services we are getting you and this is the bottom line price?"

Mr. ROVICK. Yes, Congresswoman.

Mr. RHEINGOLD. If I can add one important point here about the GMP?

Ms. WATERS. Yes.

Mr. RHEINGOLD. it is fine to do—I mean, I think it is fine to do one cost. I think the problem runs into in the subprime market the fact that there is a real interplay between the RESPA and the breakdown of costs and determining whether a loan violates Truth in Lending or HOEPA.

And if you have that one cost without any breakdown, it becomes impossible for consumer advocates and consumers to determine whether Truth in Lending has been violated. And that is an oversight in this proposal.

For instance, when someone came to my office and I was representing them—they were being faced with a foreclosure in Chicago. They would come to me and the first thing I would do is look at all of their loan documents. And I would say, "Okay, this fee looks kind of funky." But under current law, particularly Truth in Lending, which—that breakdown of fees was extremely important for me to look at because if a fee was overblown—may not have been a RESPA violation, but, in fact, it may have led to a Truth in Lending violation.

Ms. WATERS. Yes, but you are here—you are saying it is okay to eliminate that.

Mr. RHEINGOLD. No, what I am saying it is okay in a finite market—in a subset of the marketplace. I think it is okay in the prime marketplace where you are not going to find Truth in Lending violations—where you are not going to find predatory loans. I think it is very important that the GMP proposal does not remotely sink—work its way into the subprime marketplace.

Ms. WATERS. I agree. And as a matter of fact, if I am—if I have read this correctly, HUD may be suggesting that also—that it not be used in the subprime market.

Mr. RHEINGOLD. They are—they—what they said was that it should not be used for loans that are HOEPA loans. We think that the subprime market and the predatory marketplace is far below where HOEPA is and we would suggest—I know AARP has suggested—my friends at NCLCS suggested different ways to measure what a subprime loan is because it—HUD goes there, but they do not go close to far enough in making that——

Ms. WATERS. Well, is this not a good compromise to others on the panel?

Mr. BIRNBAUM. I think that if it is important to give consumers the opportunity to know what is going on that that opportunity should be available whether they are prime or subprime. And I think that the same theory applies. I mean, the typical consumer buying their house, whether they are rich or poor, is relatively a babe in the woods. And even the lawyers that are on this committee talk about how confusing these closing are.

So, to me, if this is all done behind closed doors and the lender's picking the lawyer and the title company and all these other providers, what is the check and balance? You know, maybe Ira is right, maybe in a lot of cases they do not really pay attention, but is not it at least a governor on the process to say, "well, at least you can hire your own lawyer. At least you can hire your own title company." And you do not have it done behind a curtain where the party that is picked is the one that is going to pay the most dough to get the business. It just does not make sense to me.

Ms. WATERS. Well, I do not want to jump to any early conclusions about any of this. I think we have got a lot more to learn. But I have to tell you that as we fight through this and we attempt to get some reforms that may be beneficial to the people who need them the most, I would lean on the side of making sure we protect those in the subprime market, because these are the people, for whatever reasons, are least able to do the competitive shopping and to raise questions and to do a lot of other things.

You are right, you know, the preference would be that everyone would have equal protection under the law, but if we have got to do somebody, we do the ones at the high end.

Mr. BIRNBAUM. Yes, but Congresswoman, let me respectfully suggest that in close—and we do—my company does 40,00 to 50,000 closings a year, so we see a lot of stuff from A to Z—soup to nuts kind of stuff. And the typical mom and pop—middle class, you know, qualified buyer—lots and lots of abuses go on at that level, too. So this is the American dream. And lots of people are paying too much dough because of bad lending practices. And I think that this proposed rule only exacerbates that problem.

Ms. WATERS. You are absolutely right.

And it can be, if I may, Mr. Chairman, it can be sometimes confusing. But what is interesting about a lot of the people that I try to protect is they are thrown into subprime no matter how much money they make, no matter how good they pay their bills. And so we would be able to help some people a little bit, in a different way, perhaps, get some disclosure. Because unfortunately, a whole set of people are placed into subprime lending that could be in prime lending.

So those are the kinds of considerations we have to give to this.

Mr. BIRNBAUM. And that is a good point and Ira sees it more than me, but absolutely.

Ms. WATERS. Thank you.

Chairman NEY. The point is they did not know they could have been in prime. And how do you get to that point?

I think Mr. Rheingold mentioned about sophisticated and unsophisticated and somebody else mentioned about simplification. And you can simplify, but what do you do with the unsophisticated buyer, even if it is simplified if—who is the protector or the gatekeeper or the person that works with them. I think that is a—you know, I mean simplification is great and disclosure, of course, is important, but who also helps the unsophisticated buyer? Or is it buyer beware? I mean, you——

Mr. RHEINGOLD. Well, I think part of it—part of the piece that has to sit in here is that there has got to be some teeth to the regulation, which I do not think exists in the current proposal. If, in fact, you are going to allow this guaranteed mortgage price—and I actually think that it may lower prices—if, in fact, a lender does not do—they do not comply with the Guaranteed Mortgage—they—in other words, they come up, they say, "is is what your rate—interest rate is going to be. This is what your closing cost is going to be." And at closing it changes, then there has got to be some teeth there so that there is some real enforcement—so there is an incentive for lenders not to do that.

Chairman NEY. So what is the suggestion?

Mr. RHEINGOLD. The suggestion is that if, in fact, they do not comply with the Guaranteed Mortgage Pack—if they do not comply with their promise—that initial promise, it becomes a presumption that they have violated Section 8 of RESPA. So you create a violation, because the consumer cannot prove it any other way.

I think the GFE thing—the GFE proposal is a good one because it impacts the unsophisticated consumer. Like I said, the bait-and-switch is alive and well. That Good Faith Estimate bears almost no resemblance to what you see in the end product. Making that Good Faith Estimate binding becomes very important because people, up front, know what the cost they are getting, within some limited tolerances. I think that is a good suggestion.

I think that HUD does not—but, unfortunately, as far as that proposal—this stuff gets just so complicated—the problem with that is there is no enforcement mechanism if, in fact, the end product does not match the Good Faith Estimate. It just says, "Oh, we have to give you another Good Faith Estimate." Or you have to give them something that matches.

One thing HUD can do, which is in our—in our suggestion, is simply say that if a lender gives you a final closing document that is not within the tolerances that the Good Faith Estimate is supposed to give you, then that would be considered an unfair and deceptive practice. And then you could be able to use state law to prove that they violated the law. That would be—that would be a suggestion to give it more teeth, as well.

Chairman NEY. Mr. Birnbaum, did you a——

Mr. BIRNBAUM. My experience—and, again, this is based on my own bias of where I am at and where I practice—but a good gatekeeper in our market is the lawyer that represents the client from contract to closing. I think that having an advocate for the largest financial transaction of your life is a great one. it is not true in all states, though.

And Congresswoman Waters talked about seniors—at least, you know, in California lawyers do not do closings, but at least with reverse mortgages you have to go through that counseling period. And perhaps setting a mechanism in place where, particularly in predatory lending, where people get advocacy and counseling before they get into these rip-off deals would ameliorate the problem.

Chairman NEY. I want to thank the panel.

And also the Chair notices some members may have additional questions for this panel. They may want to submit them in writing. Without objection, the hearing record will remain open for 30 days for members to submit written questions of the witnesses and place their responses in the record.

I want to thank the panel.

And I also want to thank the ranking member, the gentlelady from California, and the other members for their participation in today's hearing.

[Whereupon, at 4:56 p.m., the subcommittee was adjourned.]

A P P E N D I X

February 25, 2003

Opening Statement
Chairman Michael G. Oxley
House Committee on Financial Services
Subcommittee on Housing and Community Opportunity

"Simplifying the Home Buying Process: HUD's Proposal to Reform RESPA"

February 25, 2003

I would like to thank Mr. Ney for holding this hearing, his first as the new Housing Subcommittee Chairman.

Last October, Secretary Martinez provided the Committee with his views on the proposed reforms to RESPA. Today, I look forward to getting the perspectives from the mortgage finance industry and consumer advocacy groups on HUD's proposed RESPA reform rule.

The mortgage closing process is in great need of reform. I commend HUD's efforts to simplify the system and enhance the quality of critical information needed by America's home buyers. However, given the intense member interest in this issue last October and the attention this issue has received in the media, this issue is clearly not a simple one. Rather, it is very complex and a cautious and thorough approach – weighing all the perspectives – is very important.

I think most people would agree that RESPA, in its current form, is unnecessarily complex. HUD's proposal is intended to streamline the mortgage process and make it more consumer-friendly.

Not everyone is in agreement that the rule reaches this goal. Some have stated that the proposal would create an uneven playing field among mortgage originators, which could have several unintended consequences for industry and consumers, not the least of which is new class action litigation.

Others have stated that the big providers will get bigger, the small providers will go away and consumers will lose important consumer protections and possibly pay higher prices for services they won't even know they are buying.

On the other hand, HUD's proposed reforms to RESPA are a big step toward improving the process in which consumers obtain mortgage loans. It gives the consumers more options and would allow for lower prices. This would provide consumers with a better ability to compare prices and get the best loan available.

Secretary Martinez has provided the leadership necessary to move this debate forward. I commend him for his leadership and am confident that when the rule comes out in its final form many concerns will be addressed and consumers will benefit and the mortgage finance industry will have more flexibility to meet the technological and efficiency challenges facing our markets.

I look forward to hearing from all of you. Thank you.

STATEMENT OF THE HONORABLE
WM. LACY CLAY
Before the
Subcommittee on Housing and Community Opportunity

"Simplifying the Home Buying Process:
HUD's Proposal to Reform RESPA"

February 25, 2003

Thank you Mr. Chairman. I appreciate you having this hearing today and I look forward to the testimony that we are about to hear.

I commend HUD's effort to reform the mortgage process. Secretary Martinez and the HUD staff should be applauded for taking the initiative to amend the regulation of the real estate settlement procedures. However I am one that feels that significant changes to RESPA should be accomplished through the legislative process rather than by regulation. I think that Congress should decide how statutes that it makes should be revised, especially when the revisions are substantial. Of course this is with input from all affected parties.

Input from all parties would afford HUD the expertise of the settlement services and consumer entities that would be a tremendous resource in this endeavor.

Housing is an important sector of our national economy and is the foundation of wealth for most families. Any changes or additions to the regulations and procedures that govern the transfer and financing of residential properties must be carefully scrutinized.

There are some excellent changes proposed by HUD and some that are not so good. My biggest concern, among several, is the regulation of the subprime market. I don't feel the market has developed the required market information that is necessary for creating competitive pricing standards. Additionally, there are concerns about facilitating predatory lending. The "Guaranteed Mortgage Package Agreement" (GMPA) has an exemption that, in this Member's interpretation, would both permit and protect predatory lending practices. These are questions that must be answered and for which solutions must be put in place.

Mr. Chairman, I ask unanimous consent to place my statement in the record.

Statement of
Representative Donald A. Manzullo
House Committee on Financial Services
Housing Subcommittee

"Reform of the Home Buying Process" – The Department of Housing and Urban Development's RESPA Proposal

February 25, 2003

Mr. Chairman. Thank you very much for the opportunity to provide a statement at today's hearing.

Without a doubt, the residential real estate market is a bright spot in our otherwise uneven economy. HUD's proposal to revise the regulations governing the residential real estate settlement process is an ambitious and complex effort. While I support simplifying the process so that more first-time homebuyers can enter the market, I believe that HUD's rush to finalize its proposal may jeopardize our real estate market in the short-term. In addition, the proposal, if adopted, will make fundamental, and perhaps, irreversible changes to the process that may undermine the long-term goals of providing affordable housing and consumer benefits within the residential real estate market.

I believe that HUD has not fully analyzed and carefully deliberated all of the critical issues from its proposal. Specifically, I believe that HUD has not thoroughly considered the economic effects of the proposal on small businesses – a very important segment of our economy that has greatly contributed to the strong residential real estate market that we have today.

Pursuant to the Regulatory Flexibility Act and Executive Order 12866, HUD undertook an economic analysis of the proposal and its effects on small businesses. While the 98-page document summarizes and highlights many elements of the proposal, I believe that HUD has failed to adequately determine the economic effects on many segments of the small business community.

HUD readily admits that the small business community may lose anywhere from $3.5 to $6.3 billion annually. However, HUD does not break down the costs to each segment of the industry. There is no detailed economic analysis for the community banks – small real estate agents – small title agencies – just to name a few among the many other small businesses real estate providers not specified in the analysis.

HUD simply lumps many of the small businesses into the categories of originators and third party service providers. Without providing more detailed information, HUD has failed to follow the spirit of the Regulatory Flexibility Act and has failed to demonstrate the costs to small businesses on their industries. Without this information, it is extremely difficult for small businesses to adequately comment on the proposal. All they know is that they face billions of dollars of costs annually.

Even the Office of Advocacy of the Small Business Administration recommended that HUD publish a supplemental Regulatory Flexibility Analysis, "...to provide small businesses with sufficient information to determine what impact, if any, the particular proposal will have on [the small businesses'] operations."

I believe that the analysis raises more questions than it answers and that HUD should address these issues before finalizing the proposal. As chairman of the Small Business Committee, I will be holding a hearing on HUD's Regulatory Flexibility Analysis on March 11, to hear what the small business community has to say about it.

Before we tinker with the successful formula that has created our very strong residential real estate market, we should carefully and deliberately consider the reform proposals before us. Rushing to finalize the proposal may cause unintended, and perhaps, irreversible harm to competition in residential real estate market and prevent us from achieving meaningful consumer benefits.

Testimony of
Peter J. Birnbaum
President, Attorneys' Title Guaranty Fund, Inc.
on
HUD's Proposal to Reform RESPA

Before the
Subcommittee on Housing and Community Opportunity
Committee on Financial Services
United States House of Representatives
Washington, D.C.

February 25, 2003

Good afternoon. My name is Peter Birnbaum. I am President of Attorneys' Title Guaranty Fund, Inc., an Illinois-based title insurance underwriter. I am here today to speak with you regarding the Proposed Rule, on behalf of the National Association of Bar-Related Title Insurers (NABRTI), the national trade association of title insurance companies and their more than 15,000 attorney agents and law firms engaged in title insurance and settlement services across the country.

There is consensus within both the lending and settlement services industries that the current RESPA rules fail to adequately and appropriately address current conditions. While we agree that the present disclosure requirements are not as effective as was hoped in ensuring that consumers receive accurate, understandable and early disclosure of mortgage loan settlement costs, we are nonetheless gravely concerned that the solution proposed by HUD will worsen, not improve, the current situation. Our concerns are as follows.

First, under the guaranteed packaging proposed by HUD, borrowers would pay a lump sum for "all of the settlement services and charges required to complete your mortgage." There would be no required itemization of charges, services or providers included in the package. Presumably, this is based on the notion that consumers do not care what services they are purchasing, how much they are paying for those services or from whom those services are being purchased. This is not only contrary to our everyday experiences as consumers but it is 180° opposite from the statutory scheme that Congress adopted for RESPA. After weighing various alternatives, including a packaging proposal then called "Lender Pay," Congress determined that full and complete disclosure was the appropriate course to follow. From our perspective, disclosures to consumers should be strengthened and enhanced, not eliminated.

Second, packaging occurs under the present regulatory regime without the proposed safe harbor from Section 8 liability and truncated disclosures provided in the HUD proposal. While it is not now the primary method of providing services, it does exist. If the concept underlying packaging is valid, we are confident that the marketplace will conclude that it is a "better mousetrap" and its use will become more widespread. There appears to be no compelling reason to force HUD's version of packaging on the marketplace.

Third, the packaging that does occur today is fundamentally different than the packaging that would occur under the HUD proposal. Under the current regulations, the economic benefits of packaging discounts, or other price preferences, must be passed on to consumers. Packagers or other parties may not retain this money. If they do, it is considered a kickback and Section 8 of RESPA applies. This is not true in the HUD proposal. Packagers would be able to retain any or all of the economic benefits of packaging and not be subject to Section 8 liability if they stayed within the safe harbor created by HUD. Conceivably, none of the supposed benefits of packaging could be passed on to consumers.

Fourth, the HUD proposal does not recognize that buyers and sellers of property across the country have a long history of allocating costs among themselves. In some areas it is customary for sellers to pay the cost of title assurance. In other areas, the parties will split the cost of loan discount points. Transaction by transaction, buyers and sellers are able to negotiate how costs will be allocated. Under the HUD proposal, all of "the charges required to complete the mortgage" would be incurred by the borrower in the HUD proposed package. As a result, in some areas, the HUD package could significantly increase borrower costs.

Finally, although the Proposed Rule does not explicitly say so, the only way that HUD's packaging scheme could be implemented would be to preempt the myriad state laws, regulations and rulings that have been developed to protect consumers. Throughout our entire history as a nation, the regulation of real estate and insurance has been primarily the province of our state governments. Most states have a body of law that governs the transfer and/or insuring of real property interests. For example, many states require that all insureds be charged the same premium for the same insurance coverage. This provision is intended to ensure that all insureds are treated fairly and that some are not discriminated against or favored over others. As we understand the HUD proposal, this type of state statute would be preempted in favor of a federal regime that would likely provide widely varying costs to consumers, based only on the amount of "clout" that some larger mortgage lenders may have to get providers to give them discounts. And, of course, all of these costs would be hidden from consumers within the single package price.

While we believe that HUD should be commended for recognizing that the current RESPA statute is not as effective as we all hoped, its proposed solution would not achieve the objectives established by Congress and in fact, in our view, is at odds with those objectives. What do we have to offer as a solution to this difficult problem? We would like to propose several steps.

First, we should recognize that the process of transferring and financing of residential real estate is complicated. There is no single path by which these ends are achieved. We should further recognize that it is not realistic to assume that HUD will be able to establish and maintain a staff with the breadth of knowledge necessary to stay abreast of the constantly evolving marketplace. We suggest that HUD take advantage of the expertise found in all of the settlement services industries and the consumer movement by forming an advisory body that could act as a resource to the Department. This advisory body could act as a sounding board for HUD staff and a source of suggestions as to how the statute could be managed more effectively.

Second, we suggest that Congress direct HUD to collect and analyze information on settlement costs and practices before suggesting any further significant regulatory changes. Congress has recognized the need for data before making decisions on housing policy. In 1970, it directed HUD and the VA to study settlement costs across the country. The 1972 report of this study was a primary basis for the RESPA statute. Recognizing the need for data, Congress directed HUD in Section 14 of RESPA to report back to Congress on the effectiveness of the statute. In 1979, HUD and its contractors collected and analyzed thousands of HUD-1 forms and conducted hundreds of interviews with consumers and industry representatives. Based on these research findings, Congress elected not to accept HUD's 1983 recommendation to adopt a package regime and, instead, amended the statute in other ways. The key point is that good, solid, empirical information should be the basis for policy making, not anecdote, hunch or pre-conceived notions.

Finally, and most importantly, significant changes to RESPA should be accomplished through the legislative process, not by regulation. Housing is an important sector of our national economy and the foundation of wealth for most families. Changes that would significantly affect how residential properties are transferred and financed warrant careful scrutiny and deliberation.

Congress, and not an administrative agency, should decide whether the statutes it has enacted should be substantially revised. Indeed, the HUD proposals are essentially identical to the proposals contained in the 1998 Joint HUD-Federal Reserve report that made those recommendations as proposals for legislative amendments to RESPA.

On behalf of our members, we would welcome an opportunity to work with all interested parties to revise RESPA in a way that would make the statute more effective in meeting its objectives.

Once again Mr. Chairman, thank you for allowing me to participate in today's hearings. I would be happy to answer any questions you may have.

CONSUMER MORTGAGE COALITION

Statement Of:

ANNE C. CANFIELD
EXECUTIVE DIRECTOR

HOUSE FINANCIAL SERVICES COMMITTEE
SUBCOMMITTEE ON HOUSING AND COMMUNITY OPPORTUNITY'S

HEARING ON --

"SIMPLIFYING THE HOME BUYING PROCESS:
HUD'S ROPOSAL TO REFORM RESPA"

February 25, 2003

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Tab A

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Tab B

STATEMENT OF ANNE C. CANFIELD
EXECUTIVE DIRECTOR
CONSUMER MORTGAGE COALITION

February 25, 2003

Good afternoon. I am Anne Canfield, Executive Director of the Consumer Mortgage Coalition, a trade association of national, residential mortgage lenders, servicers and service providers. I appreciate the opportunity to speak to you today on HUD's proposed RESPA rule. We would also like to submit a copy of our comment letter to HUD on the RESPA proposal for the Committee's written record.

The CMC believes HUD's proposal represents a major step toward improving the process by which consumers obtain mortgage loans in this country. Significantly, it gives loan originators and other settlement service providers the option of offering guaranteed closing costs to consumers. And if such a guarantee is provided, it allows packagers to use their purchasing leverage to lower these costs – something which RESPA to date has prohibited. With this guarantee, consumers will have a better understanding of closing costs and be better able to shop for the best loan that suits their needs.

We also believe that this guarantee – which the proposal calls a "Guaranteed Mortgage Package," or "GMP," if structured appropriately, will help reduce predatory practices. The CMC has developed a comprehensive set of proposals to address predatory lending, which are in Tab 1 of our comment letter to HUD. The GMP is an important element of those proposals, for two reasons. First, the proposal will ensure that consumers receive relevant information about a loan's costs early in the process, which promotes comparison-shopping. Second, by simplifying the comparisons, it will increase consumer understanding and make more difficult the deception that characterizes abusive loans.

I would like to focus today on five key aspects of HUD's proposal that, we believe, are crucial to this rule becoming a reality – not just the reality of becoming a final rule, but the reality of millions of borrowers obtaining lower cost loans as a result of receiving offers of guaranteed mortgage packages.

First, the structure of the Guaranteed Mortgage Package. HUD has included in the GMP the guaranteed settlement costs and an interest rate component. Although the proposal called this an "interest rate guarantee," the interest rate is not, and cannot, be a "guaranteed rate," unless the borrower locks in the rate and qualifies for the loan. The costs to the consumer and industry of actually offering every potential applicant a "guaranteed" rate would be staggering. HUD understands this.

Because they are not guaranteed, we have urged that the interest rate and any discount points, which together constitute the interest "price" of the loan, be separated from the "guaranteed closing costs package." Consumers need to receive, and shop with, offers of guaranteed settlement costs. These costs, far more than the interest rate, are misunderstood, are not subject to comparison-shopping, and come as an unwelcome "surprise" to borrowers at the closing table. Also, if the interest "price" were removed from the package, non-loan originators would more readily be able to assemble and offer a guaranteed package because they would not have to offer the actual loan, an act that requires special licensing authority.

If HUD determines to include an interest rate component in the GMP, it must be a conditional rate, subject to underwriting. HUD also wants borrowers who have either not yet accepted a GMP offer, or have accepted but not locked in the rate, to be able to track the rate using some verifiable index. This is a problem, however, because there is no universal index that can be used to track lenders' rates. Because loan pricing is highly company-specific and is driven by numerous internal and external factors, the only way for this to work is to require loan originators to make their rates available to these applicants on a daily basis, by phone, on a website, or via some other medium. That will assure that similarly situated borrowers will be treated alike.

A few trade associations have urged HUD to adopt a "Two Package" approach to the rule. One package would be the "loan package," including the interest rate and any separate settlement charges imposed by the lender, such as loan origination or loan processing or underwriting fees. The second package would be the "settlement package," which presumably would include the remaining settlement costs, such as the title insurance, closing attorney, survey, etc. It is not clear where the costs for the appraisal or credit report would go. In some proposals, there would be a Section 8 exemption for the services within each package, but not across the packages.

After looking closely at this approach, we cannot support it because it significantly complicates the origination process, and raises more questions than it answers. Consumers want simplified shopping. They understand and shop for the interest rate, and they understand (or should understand) that they can raise or lower that rate with discount points. They now need a simple way to compare and shop for closing costs. Having certain closing costs (loan origination fee, processing fee, etc.) in one package and other closing costs (title, closing attorney charges, etc.) in another package makes it harder, not easier, to shop for these costs.

The structure we see working best is one in which lenders and other settlement service providers may assemble and offer packages of guaranteed settlement costs. If a non-lender offers a package to a consumer, it would let the consumer know which lenders have agreed to accept that package. The consumer can then go to those lenders, with that pre-approved package in hand, and negotiate for the best interest price (rate and points) he or she can obtain. The loan would still be subject to underwriting, but if it is approved, and the consumer has not changed the loan for which he or she applied, the lender and the packager would be bound to adhere to the terms of the guaranteed package agreement.

Second, the treatment of HOEPA loans. The proposal excludes from the exemption for packaging loans subject to the federal Home Ownership and Equity Protection Act, which applies to loans whose rate or points exceed specific thresholds. We strongly disagree with this exclusion. We think it is wrong to withhold from subprime borrowers the clear shopping and cost-savings advantages of obtaining GMP offers. It has been argued that many HOEPA borrowers today do not shop effectively for loans. That is all the more reason to include them under this rule. We need to give them every tool and motivation to shop. In fact, HOEPA borrowers are likely those *most* in need of GMP offers. Armed with guaranteed settlement cost offers, HOEPA borrowers can focus on obtaining the best loan price (in terms of rate and discount points) available to them in the market.

Third, federal preemption. Many state laws conflict with, or frustrate the purpose of, HUD's proposal. There are state laws that require the disclosure and itemization of all closing charges. There are state laws that, like Section 8, prohibit referral fees, or that require a direct pass-through of all third party closing charges to the third party provider, or that restrict the use of affiliated settlement service providers. An exemption from Section 8's federal prohibitions, and the express federal authority to bundle and guarantee settlement costs, will have no meaning if these state laws remain in effect. Without broad federal preemption of all state laws that conflict with or frustrate the purpose of the proposal, the advantages to consumers from the GMP are illusory. As HUD states in its economic analysis accompanying the proposal, preemption will allow "competition to substitute for regulation," which is a desired effect of providing the GMP option.

We have also urged HUD to pursue federal legislation to amplify and confirm the state preemption of these laws.

Fourth, the need to delay the changes to the Good Faith Estimate. In addition to the GMP, HUD proposed significant, new changes to the Good Faith Estimate, or "GFE," provided under RESPA. Loan originators who do not offer applicants a GMP must provide applicants with the new GFE. With the exception of the more precise disclosure of mortgage broker fees, we have urged that HUD postpone action on the GFE.

As we outlined in our comment letter, the revised GFE raises a host of compliance and operational difficulties that require significant attention. Implementing the GMP is a huge enough task. Taking on the mandatory additional project of implementing an entirely restructured GFE is too much change at once, particularly as the industry is struggling to implement the Federal Reserve Board's new requirements under the Home Mortgage Disclosure Act.

We have urged HUD to implement the GMP aspect of the proposal as quickly as possible. This is the crucial new experiment that will help consumers shop and exert downward pressure on settlement costs. However, that new process will be many months, if not years, away if HUD also requires implementation of the new GFE changes. The reason is that lenders will have to implement the mandatory changes, meaning the GFE, first. Our companies have estimated that implementation of the GFE changes alone could take upwards of 18 months. Only then will the optional GMP be implemented.

There is a second, more ominous, reason for our concern about the revised GFE. Many have argued that HUD lacks the statutory authority to implement the proposal, with the strongest attacks questioning HUD's authority to institute "zero tolerance" disclosures in the new GFE for certain categories of costs, where the RESPA statute requires only an "estimate." Lawsuits challenging HUD's authority to make these changes will only further forestall the effective date of the regulation, further delaying any benefits that would result from GMP offers to consumers.

Fifth, the need for additional legislation to harmonize RESPA and the Truth in Lending Act. In many respects, HUD is attempting to combine RESPA's settlement cost disclosures and the Truth in Lending Act's credit cost disclosures in one new HUD regulation. While there are difficulties with HUD's approach (incorporating TILA disclosures into the RESPA regulation is duplicative and causes confusion), we agree with the concept. What is really needed is federal legislation to harmonize RESPA and TILA and other federal mortgage related disclosure statutes, so that the consumer can receive one combined, coherent disclosure that covers all aspects of the loan. Such a system would vastly simplify the loan origination process for the benefit of all. Secretary Martinez has indicated a desire to pursue such legislation and we laud his efforts in that regard. We look forward to working with this Subcommittee on that much-needed legislation.

In conclusion, I thank the Subcommittee for the opportunity to testify today on HUD's bold, new proposal. I say "new proposal" with some hesitation. There's an old adage that "There are no new ideas in Washington, only old ideas that are given new labels." The idea of bundling closing costs has been around a long time. In fact, back when RESPA was first enacted in 1974, former Senator Proxmire contemplated a similar kind of simplified approach that made it easier for borrowers to shop for loans.

We believe HUD is on the right track in offering lenders and others the option of bundling and guaranteeing settlement costs, and removing barriers to competition. We should let the market work for the benefit of consumers. This is a sensible approach whose time has come. As I've mentioned before, it's also optional – allowing this new product or approach to be test marketed to see how it works. We hope that HUD's final rule allows such test marketing to begin immediately. If simplified appropriately, we think it will work and make a real, positive difference in the lives of many borrowers.

Thank you.

Tab C

CONSUMER MORTGAGE COALITION

October 28, 2002

Rules Docket Clerk
Office of General Counsel
Room 10276
U.S. Department of Housing and Urban Development
451 Seventh Street, S.W.
Washington, DC 20410

Re: Docket No. FR-4727-P-01 Real Estate Settlement Procedures Act (RESPA); Simplifying and Improving the Process of Obtaining Mortgages to Reduce Settlement Costs to Consumers Proposed Rule, 67 Federal Register 49134-49174 (July 29, 2002)

Dear Sir or Madam:

The Consumer Mortgage Coalition ("CMC"), a trade association of national residential mortgage lenders, servicers, and service providers, appreciates the opportunity to comment on the proposed amendments (the "Proposal") of the Department of Housing and Urban Development ("HUD") to Regulation X, which implements the Real Estate Settlement Procedures Act ("RESPA"). See 67 Fed. Reg. 49134 – 49174 (July 29, 2002).

We believe that the Proposal represents a major step toward improving the process by which consumers obtain mortgage loans in this country. Significantly, it removes restrictions in RESPA that have effectively prevented loan originators from offering guaranteed closing costs and from using their purchasing leverage to lower costs. With a better understanding of closing costs, consumers are able to shop more effectively for loans.

We also believe that the Proposal's guaranteed mortgage package ("GMP") concept, if structured appropriately, will help to reduce predatory practices. As HUD has acknowledged, our current system has led to the highest homeownership rate in the Nation's history. However, with constant advances in technology and mortgage delivery mechanisms, products are becoming increasingly tailored to individual circumstances. This puts a greater burden on the consumer to understand the products being offered and the comparisons that should be made to select the most appropriate loan. The GMP piece of the Proposal will help consumers in two ways. First,

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it will assist in ensuring that consumers receive relevant information about a loan early in the process to promote comparative shopping. Second, by simplifying the comparisons it will increase the likelihood of consumer understanding and make more difficult the deception that characterizes abusive loans. The CMC's comprehensive proposal to address predatory lending, of which the GMP is an important part, is set forth at Tab 1.

HUD is on the right track with the Proposal in promoting competition and letting the free market work for the benefit of consumers. However, there are aspects of the Proposal that are too complex, both for the industry and the consumer. First, any new consumer disclosure must be simple and readable — experience has shown that lengthy, complex disclosures mandated by the government are not read and are generally unhelpful.

In addition, requirements for multiple disclosures that must be re-delivered and re-accepted whenever a loan term changes draw out the entire process and add costs. As is clear from HUD's economic analysis, a primary goal and benefit of HUD's Proposal is the savings of costs. It is axiomatic that the shorter the time between application and settlement, the lower the costs of the loan.[1] Advances in technology, supported by the Federal Electronic Signatures in Global and National Commerce Act (the "E-Sign Act"), passed in June 2000, will help shorten the time needed to close mortgage loans. We urge HUD to streamline the Proposal's requirements to allow consumers and packagers alike to maximize the cost savings in these transactions.

The CMC undertook an extensive process to develop our recommendations on this Proposal. First, a CMC taskforce on the Proposal consisting of member representatives met in Washington for a 2 day session to develop preliminary positions on key issues. We then formed seven work teams to further analyze and test the viability of those positions and to suggest changes, if necessary. The teams included:

<u>Team 1. Operations</u> To review technical aspects of the Proposal affecting origination and servicing operations generally.
<u>Team 2. Wholesale</u> To review the impact of the Proposal on wholesale lending channels.
<u>Team 3. Mortgage Insurance</u> To review the Proposal's treatment of mortgage insurance.
<u>Team 4. Reg Z/B/C Coordination</u> To review the interplay of the Proposal with TILA, ECOA and HMDA requirements.
<u>Team 5. Pricing Execution (Rate Locks, Float, etc.)</u> To review the Proposal's effect on pricing, hedging costs, rate locks and floats, and execution into the secondary market.
<u>Team 6. Preemption</u> To review the Proposal's interplay with state law requirements, the need for state law preemption and the Proposal's preemptive effect, if any.
<u>Team 7. Litigation</u> To assess liability and litigation risks created by the Proposal.

The teams reported back to the taskforce in numerous conference calls and additional meetings in Washington to flesh out our final recommendations. Throughout this process, the CMC worked closely with other bank and lending trade associations, including them in our meetings and receiving their input on our positions.

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[1] Due to reduced hedging costs, etc., interest rates subject to a 15-day lock-in period, for example, are markedly lower than rates subject to a 60-day lock-in period.

model of permitting optional compliance immediately upon the publication of the final rule, with mandatory compliance in one year.

We have organized this comment in four parts, together with certain exhibits. Part I identifies issues and recommends changes to the GMP. Part II identifies concerns with the revised GFE and recommends, as noted above, that HUD postpone major changes to this disclosure. In Part II, we also support, with modifications, the one aspect of the revised GFE that should be implemented — HUD's requirement for enhanced disclosure of mortgage broker compensation. In Part III, we recommend a change outside of the GMP or revised GFE. Throughout, we refer to specific questions HUD asked in the preamble to the Proposal that pertain to the issues being discussed. In Part IV, we list and provide answers to each of HUD's questions in the Proposal in order, with references back to our more in-depth discussion of the relevant issues in Parts I and II.

In Tab 3, we have provided the complete regulatory text, black-lined to show our recommended changes. **Please note that some clarifying changes in the regulation are not discussed in the body of our comment letter; the reason for these changes should be self-evident. For example, for clarity we define the GMP guaranteed cost amount in the regulation as the "Guaranteed Loan Settlement Charge."** Similarly, in Tabs 4 and 5, we have provided revised GMPA and HUD-1 forms, respectively.

The following is an outline of the items that we comment on in this letter:

Part I: Guaranteed Mortgage Package

A. Offering and Accepting the GMP Offer

Part IV: Responses to HUD's Questions for Commenters

A. The New Good Faith Estimate (GFE) Requirements (#1-10, 29-30)

B. Guaranteed Mortgage Package Agreements (#11-28)

* * * *

Part I: Guaranteed Mortgage Package

A. Offering and Accepting the GMP Interest Rate

1. The GMP Offer Should Include a "Conditional" Interest Rate, Not an "Interest Rate Guarantee" Which is Misleading

As you know, the CMC has been working on the guaranteed settlement costs concept that would benefit consumers since 1996. We have never included an interest rate component, however, in our proposals because we believe that the settlement costs of a loan, not the interest rate, are costs that are most misunderstood, the least subject to comparison shopping, and most often come as an unwelcome surprise to borrowers at the closing table. We also note that including an interest rate component in the GMP makes it very difficult for entities that are not loan originators to offer guaranteed mortgage packages.

By altering the way loan originators offer interest rates to applicants, HUD's Proposal significantly "ups the ante" on any previous proposals designed to better inform borrowers of closing costs. What is worrisome is that the interest rate component of the Proposal, if pushed too far, will have a resounding negative effect on mortgage delivery mechanisms, with the result that the GMP becomes a regulatory experiment that is "dead on arrival."

Thus, we have concerns about the interest rate component of the Proposal. If HUD insists that it be included in the GMP, it is imperative that it be offered in a viable, economic way. The interest rate market for loans today is extremely competitive. As noted, it is our belief that, while more education and counseling are needed for the most vulnerable, consumers generally shop for interest rates. With that caveat, we offer our comments.

The Proposal defines a GMP as "a guaranteed package of mortgage related services and an interest rate guarantee for a federally related mortgage loan that is offered to a consumer under a [GMPA] in accordance with [the proposed rule]." The interest rate in the GMP is based on very basic income and credit data that a consumer initially provides under the Proposal's broadened definition of "application."

Describing the interest rate as "guaranteed" does not accurately reflect the preliminary and conditional status of the interest rate, which remains subject to final underwriting. Applicants will see the bold "Guaranteed" language on the GMP Agreement ("GMPA") and not understand the conditional nature of the interest rate. This is simply misleading. Those applicants who, upon full underwriting, qualify only for a higher rate will surely be upset when the interest rate is increased. Not only is this detrimental for customer relations, but it could very likely result in state law claims under unfair and deceptive practices statutes.

We recommend that the interest rate offer in the guaranteed mortgage package be described as a "conditional interest price (including both rate and discount points)." (We discuss below the need to disclose discount points as part of the interest charge for the loan, rather than part of the guaranteed settlement costs.) This effectively communicates to the borrower that the interest price in the GMPA remains subject to full underwriting after all relevant credit and financial information and the property valuation are obtained, and thus is subject to change.

Actually Guaranteeing the Rate is Unworkable

We want to be clear that a requirement actually to guarantee the interest rate at the time the GMP is offered is not workable. In fact, lenders will not offer a GMP if a real guaranteed interest rate must be provided to every consumer applying for such an offer for shopping purposes. Such a requirement would expose lenders to unquantifiable interest rate risk against which they cannot protect themselves and would likely be deemed an unsafe and unsound practice by financial regulators.

Unconditionally guaranteeing interest rates in shopping scenarios will result in lenders absorbing hedge costs at a level never before encountered. Under present practice, lenders hedge their pipeline of locked applications by purchasing forward commitments of money to assure that interest rate shifts will not undermine a lender's ability to deliver funds to closing as expected. The cost of these hedge instruments is a product of the expected level of pipeline fallout and the liquidity and availability of hedge instruments in the secondary market. If lenders were obligated to make interest rate guarantees available to consumers who were merely shopping, hedge costs would skyrocket and these costs would not be recovered through the assessment of lock-in fees. This escalation of hedge costs would be caused by the geometrically increased level of fallout that would occur in a shopping environment.

For example, a consumer who was shopping for a mortgage loan could utilize the Internet or other mass methods of shopping for the best GMP offer. The consumer could hypothetically obtain dozens or even hundreds of GMP offers from lenders across the country. Each lender who offered a GMP to the consumer would be obligated to hedge the "guarantee" by purchasing hedge instruments. Each lender who offered a GMP to the consumer would have a level of fallout that would be many times the fallout level that exists under the present system. The costs of such hedges in the context of increased fallout would be significant, and could initially raise interest rates by as much as 100 basis points (1%). This increase would be just the beginning, as there are not sufficient numbers of hedge instruments available in the marketplace to support the multiple guarantees that would be generated under the Proposal.

The costs of hedging are inversely correlated to the predictability of borrower behavior. For example, if we can assume a potential borrower receives five GMP/interest rate guarantees and each lender can accurately assume receipt of a one-fifth share moving to rate/lock status, then the minimum hedge cost increase would be approximately 1%. This is approximately $1,600 additional cost for each funded loan assuming an average loan size of $160,000.

There are several significant assumptions, however, which are unrealistic in this example. These include: (i) Exactly five GMPAs will be obtained by each potential borrower; (ii) the same product and pricing will be available from all lenders. (More likely there will be multiple products, prices and GMP levels.) (iii) the number of GMPs that will actually convert to a locked loan can accurately be predicted.

Lenders and other packagers, however, can offer a guaranteed settlement cost amount and can, based on the preliminary information that is provided at the time of application, provide a conditional interest rate that consumer shoppers can utilize for comparison purposes. As noted above, any move closer to an actual interest rate guarantee will severely undermine the Proposal's viability.

2. Discount Points Should be Disclosed With the Conditional Interest Rate As a Component of the Loan's Interest Price, Not Included in the GMP Cost Amount

The proposed form of the GMPA implies that each guaranteed interest rate offer is a "no point" rate or that somehow discount points are included in the guaranteed settlement costs. This is confirmed by the following statement in Chapter 5 of HUD's Economic Analysis regarding the benefits of the guaranteed approach:

> Guaranteed packaging will improve and increase borrower shopping for mortgages. Basically, guaranteed packaging reduces the loan offer to two numbers (a settlement package price and an interest rate), has zero tolerance on the package price, and guarantees the interest rate if locked (otherwise the rate varies with a market index). 67 Fed. Reg. at 49172.

We understand that having only two figures – the interest rate and a guaranteed settlement cost amount – to compare among offerings appears to simplify the shopping process. Including discounts points in the guaranteed settlement costs, however, produces effects that adversely limit consumer choice and are inconsistent with the entire theme of a guaranteed, fixed settlement cost package. It also provides the opportunity for "bait and switch."

Where discount points (or discount credits) are not separately disclosed, the applicant will not have the flexibility to choose a rate/points combination that is different from the one initially offered, a feature that many lenders currently provide to applicants and that many applicants have come to expect. Applicants today often request a different rate/points combination after applying for a loan and sometimes ask for (and receive) such a change right up to settlement. Under the Proposal, the applicant will not know whether the initially offered rate even involves discount points because they are not separately disclosed.

Tab 2 provides examples that illustrate this limitation and its potentially adverse effect on consumers. The problem is that melding discount points and closing costs together in a floating rate scenario results in <u>neither</u> of these components being fixed. Only their combination is fixed. But the consumer does not know what proportion of the total costs constitutes closing costs and what proportion constitutes discount points. This is problematic because, as shown in Tab 2, a packager's charge for closing costs available on the 1st day of a month may be different from that available on the 10th day of that month. The closing costs for new applicants are changing all the time. Thus, if only the interest rate and guaranteed costs are disclosed in a GMP offered on January 1st (without discount points broken out), a consumer accepting that GMP offer on the 10th does not know whether the actual closing costs went up and the discounts points went down, or vice-versa. Without this knowledge, it is difficult to be assured that a pricing change reflected in a reduction in discount points will be made available to the consumer.

HUD could attempt to resolve this issue by mandating that packagers keep their discount points constant in every GMP offer. This would be even more problematic, however, because it would disrupt many lenders' current pricing practices. It is not uncommon for lenders today to make small adjustments in their discount points, rather than the interest rate, when market prices move. This is particularly acute for lenders who only change their interest rates in ½ percent increments. (It would also be problematic for all FHA loans, which typically are offered only in ½ percent increments.) Forcing discount points to remain constant in a fixed guaranteed settlement cost amount takes that pricing technique away resulting in less precise pricing and, consequently, less downward pressure on interest rates. Such interference in common business practices is unwarranted.

To make the Proposal viable, discount points should be excluded from the guaranteed settlement cost amount and treated as a component of the interest price of the loan. In this case, applicants would shop on the basis of potentially three numbers: (i) interest rate, (ii) discount points (if any) and (iii) guaranteed settlement costs.

3. The GMP Should Not Include the APR and Other Detailed TILA Disclosures

The Proposal requires that the GMPA include a disclosure of the APR together with the guaranteed interest rate. In Question 20 of the Proposal, HUD requests commenters' input regarding the coordination of RESPA and the Truth in Lending Act ("TILA").

Until RESPA and TILA are harmonized by legislation, we are very concerned that HUD importation of TILA disclosures into the GMPA will cause confusion. Duplicating the APR in the GMPA could seriously confuse borrowers, particularly if the APR given in a later TILA disclosure is different. The Federal Reserve Board, not HUD, should remain the regulatory agency responsible for the APR.

Moreover, non-lender packagers, including many mortgage brokers, have no experience in calculating or disclosing the APR.[2] Including the APR as part of the GMP offer represents a major obstacle to these packagers.

[2] Currently, under Regulation Z, creditors must provide a TILA disclosure to the borrower at the same time as the RESPA GFE is required (*i.e.*, within 3 days of application) only for residential mortgage transactions (*i.e.*, loans to purchase the borrower's principal dwelling) that are subject to RESPA. For all other loans, including refinancings and home equity loans, creditors need only provide a TILA disclosure containing the APR upon consummation of the transaction. Mortgage brokers that do not close loans in their own name are not currently required to provide TILA disclosures.

We recommend that the APR disclosure be removed from the GMP offer. The complexity and uncertainty caused by an APR disclosure at this point far exceeds any benefit that it provides to the consumer. The GMP's major benefit to consumers is the guaranteed settlement cost amount, a figure which today is not shopped, is generally ambiguously understood, and is the source of unexpected, frustrating "surprises" at the closing table. In contrast, consumers today shop for and keep a close eye on the interest rate being offered and received. We urge HUD to keep the conditional interest price component of the GMP simple to assure that consumers reap the benefit of guaranteed closing costs.

Disclosures Regarding Payment Schedule, Prepayment Penalty, Balloon Payment and ARM Terms

The Proposal requires the GMPA, in Section VI of that form, to describe the terms of the loan. Specifically, the packager must indicate in this Section whether there is a prepayment penalty, the amount and due date of any balloon payment, and, if the loan is an adjustable rate loan, the initial rate, the adjustment terms, the index and margin upon which adjustments are based, the limits on periodic adjustments, and the maximum rate that can ever apply to the loan. Although the GMPA form itself does not include it, the "*Instructions for Completing the Guaranteed Mortgage Package Agreement*" state that if there is a prepayment penalty, the packager must advise the applicant that he or she may receive a copy of the prepayment penalty terms upon request. In addition, Section I of the GMPA requires the packager to identify the applicant's monthly payment for principal and interest and mortgage insurance. HUD has requested comment in Questions 20 and 25 of the Proposal regarding whether the placement of certain loan terms in the GMPA is appropriate and whether better means exist to coordinate RESPA and TILA disclosures.

Although we believe that the consumer should have the appropriate information to shop for and understand the loan, until RESPA and TILA are harmonized by legislation to allow a single loan disclosure form, we are very concerned, as a general matter, that duplicating complex TILA disclosures in the GMPA will be confusing to consumers at the very least, and cause them to ignore one or both disclosures, at worst. Furthermore, disclosing the above information will require lenders to revamp and/or alter the processes/systems that generate these disclosures, which will be both expensive and time-consuming. The cost and burden of providing such information in the GMPA is not warranted by the resulting benefit to the consumer because the borrower receives similar information in the TILA disclosure.

Thus, we recommend that HUD delete from the GMPA the following terms: the monthly payment, the terms of any balloon payment, and the information on the terms of an adjustable rate mortgage. The monthly payment is disclosed in detail in the TILA payment schedule disclosure, including not just the initial monthly payment of principal, interest and mortgage insurance premiums, but the projected monthly payments throughout the term of the loan. Moreover, the required TILA Adjustable Rate Mortgage (ARM) disclosure provides detailed information on ARM terms. These are complex disclosures that should not be duplicated on the GMPA.

The TILA disclosures on prepayment penalties and balloon payments (or a demand feature), by contrast, are very simple statements that can be duplicated in the GMPA without creating confusion or uncertainty. Again, we firmly believe that the GMPA must be "short and simple" for it to be effective. Most consumers will not read a long, complex form. Those who do have the discipline and time to read through a long form will likely be confused when they try to compare it with their TILA disclosures because they will overlap. Finally, a requirement that every loan term, or change in loan term, must be disclosed multiple times in writing draws out the entire process, which adds costs to the loan. As noted above, borrowers who are able to close their loan quickly after application receive better prices.

We recommend that the GMPA include simple, straightforward information that will confirm to the applicant the basic features of the loan he or she has applied for, as follows:

This loan ☐ does ☐ does not have a prepayment penalty.
This loan ☐ does ☐ does not have adjustable rate terms.
This loan ☐ does ☐ does not have a scheduled balloon payment.

You will receive Truth In Lending Act disclosures regarding your loan terms that you should review carefully.

4. Lock-in Fees Should Be Permitted Under the GMP

The GMP should not restrict lock-in fees. Lenders charge lock-in fees when they need to recoup the cost of reserving money at specific rates in the capital markets. Lock-in fees are unrelated to any specific settlement service. Some, but not all, lenders credit lock-in fees to other closing costs upon the settlement of the loan (in essence refunding the lock-in fee). Lock-in fees generally range from 0.5% of the loan amount (one-half of a point) to 1.0% of the loan amount (a point), but can be higher or lower depending upon the lock-in period.

Under the new GMP regime, it can be expected that the number of applications under RESPA will increase substantially with a concomitant increase in requests for rate locks. Packagers must be allowed to offset the costs of providing these rate locks with lock-in fees. To restrict these fees is a great disincentive to offering GMPs.

Lock-in fees, however, should not be included in the GMP cost amount because they are solely dependent upon the applicant requesting a rate lock. For example, where the applicant chooses not to lock the rate, but floats right up to closing (at which point the lender ultimately locks the rate, but doesn't charge the applicant), including a rate lock fee in the GMP cost amount would artificially increase this amount.

We recommend that the Proposal leave unchanged the current industry practice under which the decision whether and when to charge a lock-in fee is left to the discretion of the lender, which generally presents the applicant with a lock-in option at application.

The Proposal also should not require packagers to offer a rate lock. Many lenders have programs, particularly construction-permanent loan programs, where the anticipated closing date is uncertain and applicants are not permitted to lock-in the rate at application. Consumers appreciate these programs and the GMP should not alter the manner in which they are offered.

Lock-in Terms Disclosed in GMPA

Lenders generally use lock-in agreements to disclose to their applicants the terms of the lock-in arrangement and the fee, if any, as required by state law. As we discuss below in connection with federal preemption, the GMPA should include these terms and the state law disclosures should be preempted. This would create a federal norm for all lock-in arrangements, replacing a patchwork of state laws, many of which have no specific rate lock disclosures. To enable the applicant to compare offerings appropriately, the GMPA should disclose the amount of any lock-in fee associated with the loan product the applicant selected as an "Other Required Settlement Cost" that will be charged if and when the applicant decides to lock. In addition, the GMPA should disclose the period during which the rate lock will be effective and the circumstances, if any, under which the lock-in fee will be refunded. Finally, the GMPA should disclose that if the packager fails to close the loan within the lock-in period for reasons unrelated to the applicant, the lock-in fee will be refunded.

5. An Upfront Fee for the GMP Should Be Permissible; Fees Charged After GMPA Acceptance Should Not Be Restricted

Permissible Upfront Fee. The Proposal requires that the packager offer a GMP without charging any fee. We have already discussed the packager's need to set its own rate lock policies, including the need to charge lock-in fees, if necessary. We also recommend that HUD permit the packager to charge a fee for providing the GMP offer sufficient to cover the costs associated with providing such offer. This fee would be similar to the fee that the Proposal would allow to cover those costs incurred in the preparation and delivery of the GFE.

The need for the ability to charge an upfront fee is driven by the change in the landscape brought about by the new packaging proposal. To remain competitive and encourage applications, packagers will not want to charge such a fee. However, if packagers are deluged with applications, which is likely considering the ability to submit multiple applications electronically with the press of a keystroke, they must be able to regulate their operations by charging a fee. Processing an excessive number of applications and providing a GMP offer within three days can be time-consuming and costly. Not all applicants can be pre-underwritten quickly through an automated underwriting process. The industry is making great strides in technology which will streamline the process for many consumers, but all applicants cannot be handled by a rapid electronic process and forcing a rushed process will lead to unsatisfactory disclosures on the one hand, and unsafe and unsound decisions on the other.

We urge HUD to modify the Proposal to keep it simple and viable and let the market determine what upfront fees will be charged for offering GMPs.

Any fee charged and collected by the packager in advance of closing would be treated as part of the GMP cost amount. The fee should be nonrefundable if the GMP does not result in a closing, unless the packager chooses otherwise.

Fees After Acceptance. The Proposal allows the packager to charge a fee upon the applicant's acceptance of the GMPA. The language of the Proposal in § 3500.16(c)(3)(viii) and the reference to the payment of an "application fee" in the last paragraph of the GMPA do not limit the amount of this fee. The only limit on this fee is found in the "*Instructions for Completing the Guaranteed Mortgage Package Agreement,*" which states that the packager may require the applicant to "pay a minimal fee" upon acceptance of the GMPA. The Proposal does not provide any further guidance as to the meaning of "minimal."

HUD should make clear that upon the applicant's acceptance of a GMP offer, the packager is free to charge additional fees in advance of closing. The packager will most likely charge an advance fee for the property valuation, credit report, and other services the packager deems necessary to underwrite the loan. Some lenders today charge commitment fees upon loan approval. These fees would not be separate from the GMP cost amount, but rather are components of such amount that are merely collected in advance of closing.

6. The GMP Should Allow Immediate Acceptance of the GMPA By Telephone or Internet

Consumers increasingly shop around and apply for loans on the telephone and the Internet. Consumers frequently want to take advantage of low rates on a particular day by applying and locking in a rate that day. Some lenders today offer programs allowing applicants to lock in a rate even before a property is under contract. This flexibility enables applicants to obtain loans at very low costs.

To allow maximum flexibility to consumers to act as quickly as they desire, HUD should place no restrictions on applicants and packagers entering into GMPAs immediately over the telephone or via other electronic media, such as the Internet. As the E-Sign Act will generally allow GMPAs to be signed electronically, we focus here on telephone applications.

Assume a consumer needs to obtain a mortgage loan quickly to satisfy a condition in a sales contract. The consumer calls up a packager to apply and be approved for a loan as soon as possible. In this case, the packager should be able to describe the conditional interest price (including rate and discount point options) and the GMP cost amount over the telephone and, upon the applicant's immediate oral acceptance (which he or she provides to avoid any delays), the packager should be able to charge an application fee by credit card at that moment to order the appraisal and other required services. In this case, the packager would send out the GMPA within 3 days as a confirmation of the accepted offer.

To accommodate this situation, we recommend that HUD adopt a rule similar to the current treatment of Affiliated Business Disclosure referrals made over the phone. The packager may collect the application fee so long as (i) it provides an abbreviated verbal disclosure of the conditional interest price (including rate and discount points) and the GMP cost amount and the fact that a written GMPA will be mailed within three days, and (ii) the applicant orally accepts the GMP offer made over the telephone.

7. The GMP Offer Should Only Be Required to Remain Open for Ten Days and Should Permit the Packagers to Set a GMPA Expiration Date

The Proposal provides that the GMP must be offered within three days from the time of application. In addition, it provides that the applicant may accept the GMPA within 30 days from when the document was delivered or mailed. In Question 16 of the Proposal, HUD asks whether a 30 day time period for the applicant to accept the GMPA is an appropriate minimum time period to ensure that the applicant has adequate opportunity to shop.

We agree that the GMP offer should be delivered to the applicant within three days of application, although to conform the timing with that of the GFE, the three days should be three business days. The requirement that the GMP offer remain open for 30 days is too long. Applicants' information, particularly the credit report, can become stale in 30 days. HUD should require that the GMP offer be open for a minimum of ten days. Packagers may choose to keep the offer open longer, but we believe that ten days is ample time for applicants to shop.

Once the applicant accepts the GMP offer, subject to final underwriting, the packager should be able to require that settlement under the GMPA occur by a certain date. Today, such date would generally be the commitment expiration date set forth in the commitment or other communication of loan approval provided to the applicant once the loan receives final approval. This practice should continue to be allowed. If the applicant locks in the rate within the time frame permitted by the packager, the commitment expiration date generally would coincide with the expiration of the rate lock; otherwise the loan will be subject to re-pricing. If the applicant does not lock-in the rate, the packager should be permitted, as lenders are today, to specify a reasonable GMPA expiration date by which settlement must occur.

8. The Availability of Interest Rates on a Packager's Website or Other Accessible Media Should Satisfy HUD's "Float Rule" Because it Assures Similar Treatment of Similarly-Situated Applicants.

HUD has proposed a limit under the GMP on how the interest rate may float prior to lock-in. Basically, the interest rate may float only to reflect changes in market interest rates based on movements in an observable and verifiable index or other appropriate measure. The preamble to the Proposal states that through this requirement "HUD seeks to ensure that the rate of the loan does not vary after the borrower commits to a packager for reasons other than an increase in the cost of funds." In Question 13 of the Proposal, HUD asks what other float rule could assure applicants that the rate of a lender is not being increased to augment origination profits, and specifically asks whether a lender's commitment to constantly make rates public on a website would be a useful control.

Although, as mentioned above, the stated purpose of the proposed float rule is to ensure that the rate does not vary beyond cost-of-funds movements "after the borrower commits to a packager," the Proposal appears to indicate that once a packager offers a GMP with a rate, the adjustments to the rate must comply with HUD's new float rule both before the applicant accepts the GMP, provided the borrower accepts it within the required period, and after acceptance but before the applicant locks in the rate.

The proposed form of GMPA illustrates the proposed float rule as follows:

> This interest rate is guaranteed through settlement if you accept and sign this agreement now, and lock-in this rate by [insert date/time]. If you choose not to accept by this time, we guarantee that the interest rate will not exceed __% [over] [under] the [prime] [index] rate for __ days [30 days or greater]. If you do not accept within this period, this offer will expire. If you accept this agreement, but elect not to lock-in the rate at the time of acceptance, we further guarantee that your interest rate will not exceed ___% [over] [under] the [prime] [index] rate or other standard measure in lieu of an index when you do lock-in.

The requirement that the interest rate must float according to an observable and verifiable index is highly problematic and does not take into account numerous legitimate pricing concerns, beyond the market movement of interest rates. Most lenders today do not simply tie their pricing of fixed rate mortgage loans to external indices. Rather, lenders alter prices on a constant basis taking into account numerous factors, including the consumer demand for certain loans, what the secondary market is buying and at what price, the need to balance out their portfolio at any given point in time, the need to fill securitization pools being assembled at the end of a month, and a host of other internal policies affecting pricing. Requiring lenders to alter their pricing models and practices, we believe, would have a drastic effect on a lender's control of its own destiny. An effective pricing strategy is a valuable asset and often a competitive advantage for companies. Forcing mortgage loan pricing to conform to a simplistic formula of adding a margin to an external observable index seriously diminishes that asset in a way that could have major ramifications.

We believe that HUD's suggested alternative of the packager making its rates constantly public on a website or other widely accessible medium should satisfy HUD's concerns that an applicant who locks in a rate is treated similarly with all other similarly-situated applicants. HUD should particularly make clear that allowing the applicant to call a local or toll-free telephone number to obtain current pricing information on specific products would satisfy the rule. Many packagers may not have the systems capabilities to maintain loan package prices on a constant basis on a website. Applicants may obtain the same information quickly by telephone at a much lower strain on a packager's systems. Moreover, some applicants may not have access to a computer; virtually all applicants have access to a telephone.

We believe that the package approach, including the procedure to satisfy HUD's floating rate concerns, should work as follows:

An applicant should receive a GMPA that includes a conditional offer of an interest price (including both rate and discount points) and a GMP closing cost amount for the specific loan product for which he or she has applied. The product would be defined by various factors, including loan amount, loan term, type of rate (fixed or adjustable), type of secured property (single-family detached, condo unit, etc.), estimated loan-to-value ratio and, if applicable, the lock-in period that applies to the offered price.

To illustrate, assume a consumer applied for a packager's "alpha" product — a 30-year fixed-rate $200,000 conforming loan on a single family detached residence, whose rate is subject to a 60-day lock period. The GMP offer for that product that is effective as of the date and time shown on the GMPA includes a conditional interest price of a 7% interest rate and one discount point and a GMP cost amount of $2,000. If the applicant accepts and locks the rate immediately, which will most likely happen on the telephone, she will receive that locked-in price, subject to final underwriting and property valuation.

If the applicant either does not accept (and continues to shop) or accepts but does not lock the rate, it is important that the applicant not be treated differently from any other applicant who applied for that same product at that same time. This goal would be satisfied by having the packager publish the price of that product on its website or otherwise make that price available through another accessible medium such as the telephone on a regular, *e.g.*, daily, basis, giving both interest rate and discount points. With this information the applicant can track the price of that product and choose when to accept (if he or she has not yet accepted the GMPA) and lock-in the rate (assuming the product is able to be locked at that time). To assure that the applicant is able to track the actual rate applied for, the packager must advise the applicant to factor in any "add-ons" that affect the loan's price.

Applicants not having access to a computer to check the packager's website should be able, as they are today, to call the packager to obtain the information on its current loan prices. As noted in our recommendations at Tab 1, it is critical that HUD institute counseling and home mortgage education programs, particularly for those consumers most susceptible to abuse or who may be unlikely to shop for a loan. This education should include ways to access public computers to track mortgage prices of packagers.

Published Rates Not Advertising Under TILA

It is important that packagers be able to publish their loan prices to satisfy HUD's float rule without triggering TILA advertising requirements. Among other things, those rules require the disclosure of an APR and the terms of repayment. As noted above, many packagers are not in a position to publish an APR and it would be a significant burden to have to publish and maintain all the terms of repayment on every product a company offers. We urge HUD to recommend to the Federal Reserve Board that publication of loan prices to satisfy HUD's float rule are "notices required by law" or "cost estimates for individual consumers" that do not trigger TILA's advertising rules.[3] As noted below, we also urge HUD to preempt state advertising rules that would require a packager publishing its loan prices to disclose an APR or make some other loan-term disclosure.

[3] Under the Official Staff Commentary to Regulation Z, notices required by Federal or state law are not "advertisements" for purposes of Regulation Z if the law mandates that specific information be displayed and only the information so mandated is included in the notice. Similarly, cost estimates for individual consumers are not TILA "advertisements." Comment 226.2-2(a)1.ii.

9. The Applicant Should Receive the Chart of Options Available to Pay Closing Costs in the Revised Special Information Booklet, Not in the GMPA

The GMPA includes in Section V a discussion of the ways that an applicant may pay his or her closing costs. This is accompanied by a chart that compares the applicant's selected interest rate/points combination with other possible combinations.

We recommend that this discussion and chart be deleted from the GMPA. Instead, this information should be included in the revised Special Information Booklet,[4] which is provided with the GMPA, for several reasons. First, some lenders today do not permit applicants to buy up or buy down the rate. Consequently, this disclosure would not apply to all packagers. Second, packagers that do offer different rate/point options will be disclosing those options on its website or other accessible media to satisfy HUD's float rule. Moreover, the information on a packager's website will be current. The information on the GMPA if delivered through the mails, by contrast, may already be out of date when received by the applicant, unless he or she locked in the rate on the telephone. To further disclose hypothetical options that are also out of date will be confusing and unhelpful. Finally, including the options and chart lengthens the GMPA form that makes it less likely to be read. Again, although this last reason may not appear to be a substantive objection, in reality it is. Applicants who receive a one-page disclosure are likely to read it. Applicants who receive a 5 or 6-page disclosure are not.

It is much better to direct the applicant to the Special Information Booklet where the interaction of interest rate and points is explained in general terms. The applicant can then discuss with the packager the possible interest rate/points combinations available for the applicant's loan product. This will be more understandable under our recommendation that discount points be disclosed separately from the GMP cost amount. Finally, the explanation in the Special Information Booklet will be helpful even to applicants who have already locked in a rate because many lenders allow their locked-in applicants to select from a number of rate/point combinations on their pricing grid.

10. A GMP Offer Should Be Treated As a Pre-Qualification In Response To a RESPA "Shopping Application" and Treated as Such for Regulations B and C Because the Consumer Is Not Expecting Any Real Decision on the Loan Until After Acceptance of the Offer.

[4] In the preamble to the Proposal, HUD announced that it intends to revise the Special Information Booklet, as prescribed by Section 5 of RESPA, concerning settlement costs consistent with the Final Rule.

The Proposal broadens the existing definition of "application" under Regulation X, defining it as "the submission of credit information (Social Security number, property address, basic income information, the borrower's information on the house price or a best estimate on the value of the property, and the mortgage loan needed) by a borrower in anticipation of a credit decision, whether oral, written or electronic, relating to a federally related mortgage loan." By adding "oral" submissions to the definition of application, HUD has made clear that telephone inquiries by consumers will be treated as applications if the requisite information is provided. The definition retains the existing requirement that a specific property must be identified. In Question 28 of the Proposal, HUD asks for comments regarding the proposed definition of "application" and, in particular, its impact on other federal disclosure requirements.

By defining application so broadly, HUD is assuring that consumers may receive either a GMP offer or a GFE early in the shopping process. Because Regulation Z's definition of application is based on that of Regulation X, the borrower's submission of a RESPA application will also trigger TILA disclosures. This is consistent with the Proposal's overall goal to better enable consumers to shop.

It is important to recognize, however, that at this stage of the process the consumer is not expecting a real loan decision. While the conditional interest rate offer in the GMP is more than a simple quote of an available rate, it is not a fully underwritten rate. In this sense it is more like a pre-qualification that the consumer can use to shop. For this reason, we recommend that the definition of application in Regulation X be bifurcated between a "Shopping Application" and a "Final Application." The Shopping Application is the consumer's submission of the few items required to provide a GMP offer. It is not submitted in anticipation of a credit decision, rather it is submitted to receive a GMP offer (or a GFE in a non-GMP transaction) to aid in the consumer's shopping for a loan. The Final Application occurs once the consumer accepts the GMP offer (or GFE) and submits the additional information needed to process and underwrite the loan. At this point, the shopping phase is over and the applicant is submitting information in anticipation of an actual credit decision.

The submission of a Shopping Application should rarely be treated as an application for purposes of Regulation B and never be so treated for Regulation C. Treating every submission for a GMP offer as an application for these regulations will create severe compliance and customer relations problems and skewed Home Mortgage Disclosure Act reporting.

Under Regulation B, an "application" is defined as an oral or written request for an extension of credit in accordance with the procedures established by the creditor. Under the Regulation B Commentary, the creditor's response to an inquiry will determine whether that inquiry will be treated as an application. Thus, if a packager clearly communicates that the consumer requesting a GMP offer does not qualify for a loan, then the inquiry would likely be considered an application and such communication would constitute adverse action. Most lenders today would not deliver such an absolute communication on the basis of such preliminary information. The important point, however, is that a consumer who requests and receives a GMP offer should not be deemed to have submitted an application under Regulation B simply by virtue of receiving such offer. Under the new packaging regime, the consumer can be expected to request and receive numerous GMP offers before making a decision on which one to pursue. Once the consumer accepts a GMP offer, the packager will commence full underwriting, and the consumer now expects a loan decision. Before that, however, there is no expectation of any action and the consumer will only be confused or frustrated if he or she receives a notice of adverse action on an incomplete application or a notice of incompleteness.

Similarly, for purposes of Regulation C, the request for a GMP offer should be regarded as a "prequalification" that is not reportable on the HMDA/LAR. As noted, the consumer who receives a GMP offer from one packager is most likely making similar inquiries and receiving similar GMP offers from other packagers. These requests are akin to "a request by a prospective loan applicant for a preliminary determination of whether the prospective application would likely qualify for credit under the institution's standards." See Regulation C Commentary 203.2-Definitions, 2(b).

To this end, HUD should allow creditors to indicate in their GMP offers that a request for a GMP offer does not constitute an application for credit under either Regulation B or Regulation C unless and until the consumer accepts the GMP offer. Similar information should also be included in the revised Special Information Booklet so that consumers are aware of this distinction early in the shopping process.

Characterizing the GMP offer as a pre-qualification is consistent with the level of underwriting the packager will perform using the basic credit and income information described in the Proposal's definition of "application." The consumer is not taking the time to complete a full 1003-loan application to receive a GMP offer. Rather, the consumer is generally delivering 5 or 6 pieces of relevant information, consistent with the information needed to obtain a pre-qualification. While a packager who desires to obtain more information to develop its GMP offer should be permitted to request such information, in general no information is obtained on the applicant's assets or cash to close and there is no detail received on the applicant's debts beyond what is shown on the credit report. The GMP offer is based on a simple, preliminary credit review. This may include running the applicant's information through an automated underwriting system, if the packager has access to one, or applying the basic debt to income ratio criteria the packager uses to underwrite mortgage loans. But it should be understood for what it is and what it is not. It is in no way a full credit underwrite.

We realize that some consumer advocates would prefer that the packager perform a full credit underwrite on the applicant before offering the GMP, so that the loan approval would be conditioned solely on the verification of the applicant's initial information, the appraisal, as well as the customary closing conditions, such as evidence of clear title. First, far more information would have to be collected from the applicant, along the lines of the 1003 application form, to achieve this goal. But beyond that, the process would be so time-consuming and costly that packagers would not provide a GMP offer if they could not be compensated for the work they have performed.

We recommended above that packagers should be permitted to charge a minimal fee to provide a GMP offer, basically to be able to control the volume of applications in peak periods. However, if the packager is required to perform a full underwrite at no or minimal cost on every consumer requesting a GMP offer, making those offers will quickly become uneconomical, undercutting the incentives for, and benefits of, packaging. Under the Proposal's new regime of increased shopping and competition, packagers realize that the percentage of applicants accepting their GMP offer will be much lower in the future than the percentage of applicants who follow through with their applications to loan originators today. The benefits of packaging to consumers will be lost entirely if packagers perceive that the costs of doing the work necessary to provide GMP offers to numerous consumers exceed the benefits of obtaining some portion of those consumers as borrowers.

Allowing consumers to obtain, with extremely little investment in time and money, a GMP offer with a conditional interest price based on a preliminary credit review and a guaranteed closing cost amount is a valuable benefit, far exceeding what is provided today. Rather than undercutting the viability of the GMP concept by forcing a more complete underwrite at such an early stage, we should focus on how to get that benefit out in the marketplace as soon as possible.

Withdrawn Applications

Under current Regulation X, a lender need not provide a GFE if the application is denied before the end of the three-business-day period. We recommend this be amended to make clear that if a Shopping Application is denied or withdrawn before the end of such three-business-day period, no GMPA or GFE need be sent out.

11. All Parties to the GMPA, Including the Applicant, Should be Bound Upon Acceptance So That the GMPA Has Contractual Validity

The Proposal currently requires that upon the applicant's acceptance of the GMPA only the packager will be bound to its terms. Specifically, Section VII of the GMPA advises the applicant that once he or she accepts and signs the GMPA, the packager will be contractually bound to its terms, provided that the applicant qualifies for the loan based on the applicant's credit rating, the appraisal, and other appropriate criteria. Under the Proposal, an authorized agent of the packager must sign the GMPA. Moreover, if the packager is not a lender, the packager must have the lender sign the GMPA to agree to provide the loan. (We recommend later in this letter at item 24 that the lender not be required to sign the GMPA, but that a non-lender packager must certify that it has arrangements with one or more lenders that will accept the GMPs, subject to such lenders' underwriting and final approval of the loan.)

We recommend that the GMPA be revised to bind both the applicant and the packager to the terms set forth in the GMPA and to communicate that the terms set forth in the GMPA control. Although no packager will try to force an applicant to obtain a loan he or she does not want, this contractual agreement will help expedite resolution of cases where the applicant argues that the GMPA contains terms that are different than what were agreed to orally.

12. The GMPA Should Satisfy TILA's Itemization of Amount Financed

Under current Regulation Z, the GFE provided pursuant to Regulation X satisfies the requirement to disclose the "itemization of amount financed" under Regulation Z. We urge HUD to recommend to the Federal Reserve Board that the GMPA should satisfy TILA's "Itemization of Amount Financed" disclosure just as the GFE currently satisfies such disclosure.

Under the Proposal, a packager that meets all the requirements in proposed § 3500.16 to qualify for the safe harbor exemption can provide the GMPA in lieu of the GFE. Proposed § 3500.16(d). Indeed, under proposed § 3500.16(b), a GMP satisfies Sections 4 (regarding the HUD-1 settlement statement) and 5 (dealing with the special information booklet and the GFE) of RESPA if the conditions for the safe harbor exemption are met. In that HUD appears to regard the GMPA as fully satisfying the requirements of Section 5 of RESPA that applicants receive a GFE, HUD should have no issue making this recommendation to the Board.

Moreover, while the itemization of amount financed does indicate the non-finance charge amounts paid to other persons by the creditor on the consumer's behalf, it does not separately itemize prepaid finance charges. Rather, it lists them in a lump sum. The information received in the GMP is more helpful to the consumer to shop for a loan.

B. <u>Treatment of Specific Services and Costs Under the GMP</u>

13. The GMP Cost Amount Should Not Include Mortgage Insurance Because the Principal Determinant of This Cost – the Property Valuation – Is Not Yet Known

The Proposal includes the upfront cost of mortgage insurance (excluding reserves) in the GMP cost amount. Moreover, the Proposal states that the GMPA must "advise the borrower . . . whether the guaranteed mortgage package price includes an upfront maximum mortgage insurance premium based upon the borrower's assertion of the value of the property and the loan amount needed and that the mortgage insurance premium may decrease or be removed after full underwriting." In Question 21 of the Proposal, HUD requests comment on the treatment of mortgage insurance in the Proposal.

As a preliminary observation, the Proposal's statement that the GMP includes a "maximum" mortgage insurance upfront premium is problematic. If the applicant over-estimates the value of the property, compared with the final appraisal, the upfront mortgage insurance premium included in the GMP may be too low. Thus, if mortgage insurance is in the package, any disclosure on the GMPA regarding the amount of mortgage insurance premium the consumer must pay should state that the upfront mortgage insurance premium may "increase" as well as decrease or be removed after property appraisal and full underwriting. As discussed below, however, we recommend upfront mortgage insurance costs not be included in the guaranteed package.

We believe that the upfront mortgage insurance cost should not be included in the package because any statement of the amount of such cost at or shortly after application is too much of a guessing game. The consumer is not an appraiser. Although he or she may have a general sense of what the mortgaged property is worth, being off by 1 or 2 percent could mean the difference between needing mortgage insurance and not needing mortgage insurance or between tiers of coverage. Until a valuation is performed to the lender's standards, providing a meaningful guarantee of mortgage insurance costs to the consumer is impossible. In fact, requiring mortgage insurance to be included will result in packagers heavily discounting the applicant's assertion of value to ensure that they include any mortgage insurance cost that might be needed.

To achieve HUD's stated purpose of providing consumers with settlement costs disclosures that are as firm as possible, items that make up the settlement costs should be fixed costs. Mortgage insurance costs are subject to too many variables to be included in the package costs.

HUD indicated in Question 21 of the Proposal that one concern of excluding mortgage insurance from the package is that it represents a "major charge" to the consumer. While mortgage insurance may have been a major settlement cost in the past, it is no longer in the vast majority of cases. Most private mortgage insurance policies today are monthly-pay policies with very little, if any, premium paid upfront — typically, the only settlement charge is an escrow cushion. Thus, treating mortgage insurance as an estimated "Other Required Settlement Cost" on the GMPA should not reduce the benefit of the GMP to consumers. Moreover, the cost of mortgage insurance is fully disclosed as a component in the finance charge and APR disclosed under TILA.

To account for the uncertainty of mortgage insurance at application but still to give the consumer the most meaningful information possible, we recommend that the packager provide the applicant with [two] disclosures regarding mortgage insurance. The initial disclosure would be an estimate of the cost of the upfront mortgage insurance premium as an "Other Required Settlement Cost" in the GMPA. In addition, the GMPA would disclose the packager's policy for requiring mortgage insurance (i.e., when the loan-to-value ratio is 80% or greater), and a statement that the estimate, of any, of the cost of upfront mortgage insurance is based on the loan's loan-to-value ratio calculated from the applicant's assertion of the value of the property.

No later than 30 days after the applicant accepts the GMPA, during which time the packager will obtain an evaluation of the property, a final mortgage insurance costs disclosure would be provided to the applicant including: (i) the final amount of the upfront mortgage insurance premium, and, in cases where the final amount exceeds the initial estimate in the GMPA, the reason(s) why the final amount exceeds the estimate; and (ii) a statement that the upfront mortgage insurance premiums collected at settlement (not including reserves) will not exceed the final amount of such premiums in the disclosure, unless the applicant subsequently requests a change in the amount or terms of the loan.

If the packager provides this second disclosure, and the costs of mortgage insurance at closing do not exceed the final amount of such costs as disclosed, the Section 8 exemption should apply to the packagers arrangements with mortgage insurers for insurance.

To further ensure that consumers fully understand the role of mortgage insurance in the loan process, we recommend that information regarding mortgage insurance and its costs should be included in the Special Information Booklet, which HUD indicated that it would revise to be consistent with the final rule. The marginal benefit of disclosing on the GMPA what portion of a loan's APR is attributable to mortgage insurance is far outweighed by the costs of calculating and providing such information and the additional complexity it adds to the model GMPA disclosure, particularly given the uncertainty of the information pending the receipt of the property's appraised value. Information that gives the consumer a general sense of the additional cost of mortgage insurance over the term of the loan is best included in the Special Information Booklet.

14. The GMP Price Should Not Include Flood Insurance Because the Determinant of This Cost – the Flood Search Report – Has Not Been Ordered or Performed

Under the Proposal, flood insurance is included in the GMP cost amount. Although we agree that this amount should include the cost of a flood certification, we urge HUD to exclude flood insurance from the package cost because, like mortgage insurance, this is a service that may or may not be required to be purchased, depending upon whether or not the property is located in a flood zone, as indicated by the flood search report, once that has been ordered. Like the appraisal, the flood search will not be ordered or performed until the applicant accepts the package. The packager clearly will not know whether it will be required or how much the insurance will cost until it receives this report.

In addition, like hazard insurance, flood insurance is often purchased separately, outside of the loan transaction, and the consumer can choose the deductible, which affects the final cost of the insurance. For these reasons, we recommend that HUD treat flood insurance as an "Other Required Settlement Cost" on the GMPA.

15. The GMP Cost Amount Should Not Include Charges Payable In a Comparable Cash Transaction

The Proposal defines the GMP not by delineating specifically what services are included in it, but by including in the package all services the packager requires for settlement, except for certain specified items that are excluded from it.[5] Thus, for example, by not excluding them, HUD has included mortgage recording taxes and charges in the guaranteed package cost. Our members believe that they can accommodate the inclusion of recording taxes and charges in the GMP cost amount, provided that the rule makes clear that changes in the loan amount, which determines the taxes and several other charges, will result in changes in the GMP cost amount. However, this issue points to a more significant clarification that must be made.

The GMP cost amount should not include any charge that is payable in a comparable cash transaction. Thus, while mortgage recording taxes and charges are in the GMP cost amount, transfer taxes paid on the recorded deed in a purchase transaction or property taxes that are apportioned in a purchase transaction should not be. This is consistent with TILA's definition of a finance charge. Under TILA, finance charges are defined generally as any charge required by the creditor as a condition of the extension of credit, excluding any charge "of a type payable in a comparable cash transaction." See Regulation Z § 226.4(a).

5 See Proposed § 3500.2(b) (defining "packaged services" as "settlement services that the lender requires for settlement and includes all services except per diem interest, hazard insurance, escrow/reserves, and optional settlement services").

Itemizing Taxes for IRS Purposes

We recommend that HUD not require the packager to break out recording taxes and charges for purposes of the borrower's tax deduction. Packagers will take this step on their own as necessary to accommodate their borrowers.

16. The GMPA Should Not Include Costs Required to Satisfy Underwriting or Closing Conditions That Are Not for Settlement Services

The Proposal should clarify that the GMP cost amount does not include costs that are required to satisfy underwriting conditions or closing conditions, but that are not for settlement services necessary to obtain the loan. For example, a lender's underwriting condition for a newly constructed residence may include obtaining a certificate of occupancy. In some cases, obtaining this certificate will require payment by the applicant of a subdivision assessment, which the closing attorney may collect at or before closing. This payment, however, should not be in the package because it is necessary to satisfy a customary closing condition and is not a cost for a settlement service.

Another example is the cost of an environmental audit. If, for example, the appraiser noted some possible contaminated soil on a rural property resulting from some underground storage tanks, the lender could rightly refuse to approve the loan until it receives a Phase 1 environmental report on the property. The cost of this report is necessary to satisfy an underwriting condition and is not for a settlement service. Lenders must be able to assume that the properties securing their mortgages comply with local laws and ordinances, including environmental restrictions. Costs to assure such compliance should not be included in the GMP cost amount.

A further example is the cost of paying off, releasing or subordinating prior liens. These amounts are not for settlement services, but are required to meet the closing condition that the new mortgage is in a first-lien position on the secured property.

Finally, costs due to unforeseeable and extraordinary circumstances, including acts of God, war, and other disasters, should not be included in the GMP cost amount. It is unfair to put the entire burden of these types of costs, whatever they might be, on the packager. As is done today, the lender and the applicant will have to work out how to handle these unforeseen costs on a case-by-case basis.

17. It Is Unnecessary for the GMP To Include a 10% Tolerance on Escrows Because of Existing Regulation X Rules

The Proposal excludes amounts charged for reserves/escrow from the GMP cost amount, but requires that an estimate of the reserves/escrow charges be included in the GMPA. The Proposal subjects estimates of reserves/escrow to a ten percent tolerance, absent "unforeseeable and extraordinary circumstances" defined as "acts of God, war, disaster, or any other emergency, making it impossible or impractical to perform." Proposed § 3500.2(b). If these circumstances exist and cause the escrow to exceed the amount estimated in the GMPA by more than ten percent, the packager must retain documentation of these circumstances for five years after settlement. Proposed § 3500.10(e). Presumably, this ten percent tolerance on the estimate of amounts charged for reserves/escrow reflects intent to deter lenders from abusing the use of reserves/escrow by collecting greater payments to the reserves/escrow account than are necessary.

First, we are not aware that this has been a notable area of abuse, particularly since HUD clarified its escrow rules under Section 3500.17 of Regulation X to require aggregate accounting.

Second, we believe that the tolerance is unnecessary in light of HUD's existing escrow rules regarding the amounts that may be collected at settlement under Section 10 of RESPA. Imposing a separate tolerance will not yield greater accuracy in the estimates of the reserves/escrows. In addition, a tolerance for reserves/escrow is problematic because such estimates vary widely depending on the settlement date and loan originators will have to factor in and track changes in property taxes and insurance rates, information that many loan originators may not possess.[6] Some escrow items, such as escrows for taxes on new construction, are impossible to estimate consistently with precision. For example, this information varies based on property values and there are factors affecting these values, such as changing tax assessments that are wholly outside of the packager's control and in some cases knowledge. In other cases, the packager's knowledge comes after the GMP is offered. As noted above, whether a packager need even include reserves for mortgage insurance will depend upon the valuation of the property obtained by the packager. A packager estimating reserves based on the applicant's assertion of the value of the property being financed, under which assertion no mortgage insurance is required, should not be held to a tolerance when the valuation of the property subsequently obtained by the packager shows a lesser value which triggers the need for mortgage insurance.

Also, a tolerance is unnecessary because consumers will generally not use reserves/escrow as a basis for shopping inquiries because in most cases these items should generally be the same for all packagers. These amounts will differ only in unusual cases where, for example, lenders may use a different escrow cushion.

Rather than include a tolerance for reserves/escrow, we recommend that the GMPA disclose that these items should not vary from packager to packager, absent unusual circumstances. Moreover, the Special Information Booklet should urge applicants who are comparing packages to specifically question a packager's reserves/escrow estimated amount that differs from the estimates of other packagers.

If HUD determines to keep the tolerance on reserves/escrow, servicers would need to conduct an escrow analysis immediately after closing and increase the reserves/escrow as needed to address any escrow deficiencies or shortages pursuant to RESPA's existing escrow rules.

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6 See HUD's final rule adopting aggregate escrow requirements, expecting servicers rather than originators to provide the initial escrow analysis because of the expectation that servicers are more likely to have accurate information. 59 Fed. Reg. 53893.

18. Disclosure of Anticipated Ordering of Credit Report, Pest Inspection, Appraisal, or Lender's Title Insurance

The GMP gives packagers the freedom to decide on a case-by-case basis which services are required for each mortgage loan. Accordingly, the Proposal does not require packagers to itemize settlement services included in the GMP. Section II of the GMPA expressly informs borrowers that "[t]he precise services for each transaction may vary."

The CMC strongly supports this approach. Lenders today commonly forego the traditional settlement services required to originate a loan as both portfolio investors and securitizers reassess the value they place on appraisals, title insurance, and other common settlement services. More and more, lenders are obtaining automated alternatives to traditional services, such as automated valuation systems in lieu of traditional appraisals for certain low risk loans. Similar alternatives are being developed for title examinations and title insurance. The Proposal encourages packagers to continue developing these more cost-effective systems, with consumers the likely beneficiaries of the reduced settlement costs.

HUD has requested comment in Question 17 of the Proposal regarding whether packagers should be required to inform the applicant whether the packager anticipates obtaining items such as an appraisal, lender's title insurance, a credit report, or a pest inspection. Attachment A-1 of the GMPA further stipulates that the applicant is entitled to a copy of any of these reports, presumably, although the form does not specify this, free of charge. HUD believes that these services are of specific interest and value to the applicant in making choices, such as, for example, whether to purchase owner's title insurance.

We understand the need to strike a balance between maintaining the integrity of the package approach and providing the consumer with useful information. We believe, however, that this requirement should be modified to adhere to the packaging concept more closely, and that this can be achieved without sacrificing useful consumer information. It should be sufficient for the packager to inform the consumer that he or she may inquire whether the packager has obtained a lender's valuation of the property, a lender's inspection of title, credit verification, or a pest inspection, using these specific terms. Packagers will compete, in part, on whether they provide additional useful items for the consumer. With the exception of the pest inspection, which generally is a condition of the sales contract in any event, we do not think that those packagers should be required to deliver these items. It is important that the consumer understand that all items obtained by the packager to make the loan are for the packager, not the consumer.

With respect to the appraisal, the applicant already can obtain a copy of the appraisal or other valuation upon request in accordance with the procedures set forth in Regulation B, Section 202.5a. This requirement does not need amplification.

With respect to title insurance, we believe that whether the packager provides a copy of the packager's title inspection should be at the packager's discretion, not a requirement of the safe harbor exemption. The packager should inform the applicant, if asked, that a title inspection was performed and whether title insurance was obtained that may affect the applicant's cost of obtaining owner's title insurance. The packager, however, should not have to provide a copy of the title inspection report or title insurance obtained. Often these title inspection reports include copies of documents, such as utility easements, that are referred to in the report. Other reports may be based on internal proprietary systems. The packager's title inspection and/or insurance are obtained for the packager, not the consumer.

With respect to credit verification, HUD should not require packagers to reveal which credit verification procedures they use, because in many cases these are proprietary underwriting tools. For similar reasons, HUD should not require packagers to provide the reports they use to make underwriting decisions. Packagers obtain and generate various credit information in various formats to underwrite the applicant's credit, ranging from a simple commercial credit score to an internal and proprietary mortgage score to a full standard, factual credit report obtained from one or more credit bureaus, with many variations in between. Section 609 of the Federal Fair Credit Reporting Act ("FCRA") already gives consumers access to their credit file information to ensure that the information is accurate. But FCRA does not require credit bureaus or creditors to provide credit scores or any other risk scores or predictors relating to the consumer. In fact, many contracts with credit bureaus expressly forbid the creditor from handing out credit scores. HUD should not effectively expand FCRA by requiring packagers to reveal their credit verification procedures or reports used in underwriting.

With respect to the pest inspection, we believe it would be very useful for the applicant to be able to obtain a copy of the pest inspection used by the packager, even though a pest inspection is a condition of a home sale and the inspection is generally ordered and paid for by the seller. In refinance transactions, the packager may not require a pest inspection. However, we believe a lender or other packager should comply with an applicant's request for a copy of the pest inspection. Packagers should be able to make clear, however, that the pest inspection was obtained for their purposes in underwriting the loans and that they have no responsibility for the pest inspection in any respect.

Overall, the above-recommended approach will keep origination costs down, which is the goal of packaging. The expense of requiring packagers to provide free reports on all these items (except the appraisal, which is covered by Regulation B and the pest inspection), and of monitoring compliance with such requirement, should not be underestimated. In this case, in addition to the more substantive reasons set forth above, the expense of creating systems to make the determination of what reports or items to deliver in each loan outweighs the usefulness to the consumer of having the information and reports. The consumer really just wants to know whether these items were obtained.

In light of the foregoing, we recommend Attachment A-1 to the GMPA be deleted.

19. Applicant Requests of Providers Not Covered By GMP

The Proposal is silent on the treatment of settlement charges in the GMP in situations where the applicant requests that a particular provider, such as closing attorney, be used. Where the requested provider differs from the one the packager planned to use, the costs of such provider may increase the GMP cost amount. These requests generally are inconsistent with the packaging approach under which the packager selects and negotiates with the providers participating in the package. However, lenders and packagers should be able to honor these requests without losing the safe harbor exemption.

We recommend that the Proposal provide packagers the option of allowing the applicant to select a specific settlement service provider other than the packager's provider. In such case, the applicant must pay the charges of the applicant's selected provider separate from the GMP cost amount. Obviously, the packager is free to reduce the cost of the package, if it deems appropriate under the situation, but no reduction in such cost amount should be mandated. The packager may be using average cost pricing with its customary vendors that will make it very difficult to compare prices with an applicant-selected provider on any individual loan.

C. Scope of Safe Harbor Exemption

20. The Safe Harbor Exemption Should Be Applicable to HOEPA Loans Because HOEPA Borrowers Are Those Most in Need of a GMP Offer That Reduces Costs and Enhances Shopping

The Proposal excludes from the safe harbor exemption high-cost loans subject to the federal Home Ownership and Equity Protection Act ("HOEPA") or for loans that HUD may, during the course of this rulemaking, deem as not suitable for the safe harbor exemption. HUD has requested comment in Question 15 of the Proposal regarding whether the exclusion of HOEPA loans, or any other loans, from the safe harbor exemption is appropriate.

The CMC believes that excluding HOEPA loans from the safe harbor exemption is inappropriate. There is no reason to withhold from HOEPA loan borrowers the clear shopping and cost-savings advantages of obtaining GMP offers. As discussed above, the safe harbor exemption allows packagers to bring their purchasing leverage to bear on settlement costs and to guarantee their amount up front. To the argument that many HOEPA borrowers today do not shop effectively for their loans, we respond that the ability to receive GMP offers may be the best way to motivate them to shop. In fact, HOEPA borrowers are likely those most in need of GMP offers. Armed with guaranteed settlement cost offers, HOEPA borrowers can focus on obtaining the best loan price (in terms of rate and discount points) available to them in the market.

HOEPA and State Law *"Points and Fees"* Issue

We are particularly concerned about a specific issue that could result in many prime loans being inadvertently treated as HOEPA loans as a result of packaging. As HUD is aware, one of the triggers of HOEPA is if the "points and fees" charged to the borrower equal or exceeds 8 percent of the loan amount (8 points). Under § 226.32(b) of Regulation Z, "points and fees" includes, among other things, "all items listed in § 226.4(c)(7) (other than amounts held for future payment of taxes) unless the charge is reasonable, the creditor receives no direct or indirect compensation in connection with the charge, and the charge is not paid to an affiliate of the creditor." Section 226.4(c)(7) charges include, among other things, the following fees, if bona fide and reasonable in amount: (i) fees for title examination, abstract of title, title insurance, property survey, and similar purposes; (ii) fees for preparing loan-related documents, such as deeds, mortgages, and reconveyance or settlement documents; (iii) notary and credit-report fees; and (iv) property appraisal fees or fees for inspections to assess the value or condition of the property if the service is performed prior to closing, including fees related to pest-infestation or flood-hazard determinations.

Notably the § 226.4(c)(7) fees are precisely those types of fees that are covered by the GMP cost amount. If these fees are treated as direct or indirect compensation to the creditor or as paid to an affiliate of the creditor, they will all be counted toward the HOEPA points and fees test, rendering many prime loans subject to HOEPA's provisions.

In addition to HOEPA, many states have high cost loan laws with "points and fees" thresholds that are lower than HOEPA's 8 points. Packaging should not inadvertently convert loans that would not ordinarily trigger these laws into high cost loans that must comply with these laws' increased disclosures and more restrictive provisions.

This issue must be clarified. The difficulty is that under the packaging approach lenders and other packagers will have situations where their GMP cost amounts will not be based on transaction-specific costs for vendors' services. A packager may find it advantageous to agree with an appraisal management company, for example, to pay an annual sum in advance for all its appraisal orders for that year. The next year, the parties will reset the annual sum based on the experience (the number of appraisal orders, the quality of the work, etc.) in the previous year.

We recommend that packagers be able to exclude amounts from the GMP cost figure, for purposes of calculating the "points and fees," so long as they have a reasonable basis for doing so. For example, a packager who pays an annual sum of $100,000 to an appraisal management company upon the expectation that it will order 1,000 appraisals from the company during the year would have a reasonable basis for excluding $100 from the GMP cost amount for each loan it originated that year. We urge HUD to recommend this solution to the Federal Reserve Board.

The uncertainty that this situation creates, however, is another reason to make the safe harbor available to HOEPA loans. To not do so creates untenable risks for lenders who, when making any loan with a GMP cost amount that nears the applicable threshold, will not know whether it is protected by the safe harbor exemption.

21. The Scope of the Safe Harbor Should Be Clarified and Provide for a Cure Provision To Avoid Unnecessary Loss of the Section 8 Exemption Due to Non-Material Mistakes

The Proposal's safe harbor exemption from Section 8 of RESPA provides that "[a] Guaranteed Mortgage Package, including any payment, discount, pricing arrangement or any other exchanges of things of value by and between persons or entities offering their services and compensated through guaranteed mortgage packages (hereinafter "packagers") and participating settlement service providers as part of such transaction, shall not violate Section 8 of RESPA ... if the conditions set forth in this section are met."

The safe harbor covers the cost of the GMP charged to the borrower, which deters potential allegations that whatever deals between the packager and the service providers individually or collectively constitute an unearned fee under Section 8(b) of RESPA. In addition, the exemption covers any exchanges of value between packagers and "participating settlement service providers," defined as those providers that provide settlement services in a GMP and whose charges are included in the GMP price.

In Tab 3, we recommend several wording changes to the language of the safe harbor, as well as to the definition of participating settlement service provider that, we believe, makes the application of the safe harbor clearer. Among other changes, we clarify that –

- Even where the guaranteed mortgage package price is zero, as in a no-cost loan, the participating settlement service providers who provided settlement services for that loan are still covered by the safe harbor exemption.
- The safe harbor exemption covers arrangements and payments between a non-lender packager and the lender, as well as payments between each of those entities and the participating settlement service providers.
- The loss of the safe harbor exemption because of an un-cured over-collection of guaranteed loan settlement charges should only affect the packager and the settlement agent. Participating settlement service providers acting in good faith should not lose the exemption because they do not control the amounts collected at settlement and will likely never be aware that a violation of the safe harbor conditions has occurred.

The other changes to the safe harbor provisions are self-explanatory.

HUD has requested comment in Questions 11 and 12 of the Proposal regarding whether the proposed scope of the safe harbor is appropriate and whether a provision allowing for volume discounts and/or mark-ups when a package is involved is sufficient to enhance competition, lower settlement costs for borrowers and simplify the mortgage shopping process.

We do not believe a narrower exemption allowing for volume discounts and/or mark-ups would be appropriate for this rule because it would unduly restrict packagers in their negotiations with their settlement service vendors. It is true that, if only volume discounts and mark-ups were expressly permitted, packagers could freely exchange promises of a greater volume of orders to a settlement service provider for discounts on the price. Because vendors usually achieve some economies of scale from a greater volume of orders, they would likely agree to this exchange. This would exert downward pressure on the lump sum closing costs amount that packagers offer consumers to meet market competition.

Such a narrow exemption, however, is insufficient because it unnecessarily constrains the range of possible packager/vendor negotiated arrangements, and needlessly creates uncertainty for any variant from a simple agreement that fits the express, narrow exemption. How would such an exemption apply to an arrangement, for example, that required a vendor to supply a second settlement service (*e.g.*, a flood certification) to a packager "for free" every time the packager ordered the initial service (*e.g.*, an appraisal). Is that second service a "discount"? What if that second service is not a settlement service, but just a valuable service or good to the packager (*e.g.*, additional industry or marketing data)? Or how would such an exemption apply to an arrangement that required the vendor to defray certain costs of a packager depending upon the volume of orders received, but the costs were not loan specific costs? How related must those costs be to the service provided? None of these questions is clearly answered by a narrow exemption.

The fact is that there are numerous mutually advantageous, economic arrangements packagers can enter into with third party service providers and there is no reason to limit them to a simple "if you give me volume, I'll give you a discount" negotiation. If it is of more value to both parties to reach a different agreement, they should be able to do so, as long as the packager guarantees the total costs to the borrower. Value, like money, is fungible. A volume discount is no more and no less a thing of value than a second free service or a reimbursement of a packager's cost. The goal is to create an incentive to have packagers offer guaranteed closing costs. To reach that goal, the exemption must be clear and certain. Otherwise, any negotiation that varies an iota from the straight volume discount model will be subject to a needless cloud of legal exposure under Section 8.

Cure Provision

The CMC has two additional principle issues with the structure of the proposed safe harbor. First, if the GMPA contains all of the information that HUD proposed, including information that overlaps with TILA disclosures, such as of information regarding monthly payments, APR, ARM loan information and so forth, any small error in those disclosures could result in the loss of the exemption. As noted above, we strongly recommend that this information not be required in the GMPA. If our recommendations are not followed, however, the safe harbor exemption should be available to packagers and participating settlement service providers as long as the one, guaranteed material disclosure – the amount of the guaranteed settlement costs – is honored at closing. The interest price is not guaranteed so it can vary. But the heart of the GMP is the guaranteed costs. It would be unfair, we believe, to deny the exemption to a packager because the monthly principal and interest and mortgage insurance premium for one of the options on the chart is off by a few dollars or because the packager delivered the GMPA within 4 business days, not 3, of the application. These are not material errors for purposes of the exemption.

Second, even on one loan, the loss of the safe harbor exemption could result in significant liability. The damages for violating RESPA equal three times the amount of settlement services involved. In this new disclosure system, plaintiffs can be expected to argue that the damages should be equal to three times the guaranteed mortgage package price.

To address this concern, we believe there should be an opportunity to cure honest mistakes without losing the exemption. For example, if a closing agent inadvertently charges $10 more for an amount that should have been in the package, the packager should be able to review that loan and refund the money without losing the exemption. Specifically, the rule should contain a cure provision that provides that: (i) the packager may cure a mistake it discovers on its own without penalty for 90 days from the date of closing by refunding any payment in excess of the costs agreed to under the GMPA; and (ii) if, after the 90 days, the borrower discovers a mistake, the packager will refund double any excess payment under the GMPA. The cure provision would apply for up to one year from the date of closing. As long as a packager complied with the cure provisions, the packager would not lose the safe harbor exemption. This cure provision would not be available to any loan originator that engaged in a pattern or practice of willfully and fraudulently charging amounts that exceed the guaranteed cost amount.

22. Arrangements Covered By the Safe Harbor Exemption Should Not Taint Loans Originated Using the GFE

Under the Proposal, Section 8 of RESPA remains applicable to payments by and between packagers or participating settlement service providers and parties outside the GMP. The preamble to the Proposal notes, for example, that a real estate agent, outside of the package, would continue to be subject to Section 8 for accepting a payment from a packager for referring a consumer to a package. Referrals to a packager by an affiliate of the packager that is not participating in the GMP remain subject to the affiliated business exemption requirements. HUD has requested comment in Question 12 of the Proposal with respect to how the safe harbor exemption should apply to affiliated business arrangements to protect consumers from steering.

Packagers will encounter significant compliance difficulties when they deal with settlement service providers who are included in a GMP in one transaction but not in another. For example, a packager offering GMPs on a regular basis may occasionally originate a loan under the GFE, to which the safe harbor exemption will not apply. It appears inevitable that consumers will end up being charged one price for a service on a GMP loan and another (higher) price for the same service in a GFE loan. This situation cannot be allowed to become a basis for litigation or enforcement.

If a packager ensures that any arrangements it makes with its service providers in connection with loans originated under a GMP do not apply to GFE loans, HUD should make clear that the safe harbor exemption is absolute and the arrangements covered by the exemption may not be used to challenge referrals to service providers in connection with GFE loans.

The critical point is to prohibit a plaintiff challenging a GFE transaction for Section 8 violations, or a court hearing such claim, to consider any aspect of the GMP deals offered by the packager as part of the challenge. For example, a claim that the GFE service costs more due to the fact that the parties have a package deal should not be allowed as an argument in any forum.

With respect to affiliated business arrangements, HUD should not be concerned that the use of these arrangements would somehow undermine the GMP or result in adverse "steering." The rationale behind the GMP is that packagers can make whatever arrangements with settlement services providers they deem necessary, either through volume-discounts, affiliated business arrangements, other incentives, etc., as long as in the end, the packager provides the applicant with a guaranteed settlement charges. The background negotiations that yield the GMP price are irrelevant. Providing packagers with the freedom to negotiate in any manner with settlement service providers so as to offer consumers with a competitive, yet simplified, marketplace for mortgage shopping is the precise point of creating a safe harbor exemption for GMPs that comply with HUD's requirements.

D. Coverage of GMP and Qualifications of Packagers

23. The GMP Should Apply to Home Equity Lines of Credit ("HELOCs") to Allow Consumers to Better Compare Prices and Shop for the Best Deal

The GMP provisions of the Proposal do not clearly apply to HELOCs. The Proposal merely states that HELOCs subject to Truth in Lending Act ("TILA") requirements remain exempt from RESPA's GFE and HUD-1 requirements, as Regulation X currently provides. 24 CFR 3500.7(f). In Question 26 of the Proposal, HUD asks for comments regarding whether the GMP should apply to HELOCs. We believe the GMP provisions of the Proposal should apply to HELOCs.

Consumers generally obtain HELOCs in two scenarios, either as a so-called "piggy back" HELOC at the time the consumer obtains a first mortgage loan or as a "stand-alone" HELOC, which is obtained independent of a first mortgage loan. In both cases, but particularly in the second case, consumers should be able to receive a GMP to assist them in shopping for the best available HELOC. Although HELOCs typically have fewer costs than first mortgage loans, consumers should still compare prices and costs when determining which HELOC to obtain. By including HELOCs in the GMP, the mortgage process for these consumers will be both clearer and less complex due to the more shoppable settlement costs disclosures provided by the GMP.

In addition, many lenders today use the same vendors for HELOCs as they do for closed-end mortgage loans, particularly with respect to "piggy back" HELOCs. There is no reason not to allow lenders and other packagers to negotiate for lower costs with these vendors on HELOCs the way they will for closed-end mortgage loans. In fact, treating HELOCs differently would cause compliance difficulties in the common situation where a packager uses the same settlement services, such as appraisal, credit report and closing services, for both a first mortgage and a "piggy back" HELOC closed at the same time. Assume the packager negotiated a volume discount with its vendors for these services. Although Section 8 would not apply in the first case, it would in the second case and the volume discount would be impermissible. The Proposal should permit packagers to offer GMPs to consumers and freely negotiate with their vendors for lower costs in both cases to reduce settlement costs.

We do not believe that conforming the GMP forms to incorporate HELOCs would be burdensome. Most HELOCs are variable rate loans whose rates are based on the lender's prime rate, which changes from time to time. This is no different from many construction-permanent loans, which are covered by RESPA, where interest during the construction phase is often based on the lender's prime rate. For these construction-permanent loans and HELOCs, then, the preliminary interest rate would simply be stated as the initial rate. We discussed in detail above our suggested changes to the interest rate guarantee.

24. Non-Lender Packagers May Offer the GMP Credibly Without Additional Financial Requirements.

The Proposal provides that the term "packager" means a person or entity that offers and provides GMPs to borrowers. HUD makes clear that entities other than lenders may be packagers that qualify for the safe harbor exemption, as long as they satisfy the requirements of the rule. In Question 18 to the Proposal, HUD asks for comments regarding the need for additional protections for packaging.

The CMC supports HUD's decision to allow entities other than lenders to offer GMPs. Concerns regarding the financial net worth of a packager are addressed by the fact that lenders will engage in their own due diligence processes to approve packagers with which they will offer GMPs and set their own standards for dealing with a packager. We do not recommend a codification of those processes, which would be burdensome for lenders and impossible for consumers to ascertain.

We also recommend changing the regulation to remove the requirement that non-lender packagers have to obtain a lender's signature on the package. Packagers, especially mortgage broker packagers, should be able to enter into a binding and enforceable contract with an applicant to provide a loan without the need for a lender's co-signature. At the same time, we recognize that consumers need to know that their packager, if not a lender, has made arrangements for a lender to fund the loan being offered in the GMPA, if the consumer is ultimately approved for the loan. To this end, we recommend that the GMPA include a certification by all non-lender packagers to the effect that the packager has entered into arrangements with one or more lenders to which the packager's GMPs will be acceptable, subject to such lenders' underwriting and final approval of the applicant.

If the final rule retains the requirement for a lender signature on the GMPA, the rule should allow the lender to provide a separate disclosure to the consumer evidencing its assent to the package, rather than actually obtaining the GMPA signed by the broker or the consumer and adding its signature, which would be logistically difficult. In addition, the lender, if it chooses, should be allowed to add a disclaimer to the effect that the lender's signature commits it to provide the terms represented in the GMPA, but does not make it responsible for any actions of the mortgage broker or other non-lender packager.

25. Packaging Should be Limited to Persons or Entities Able to Engage in Primary Market Activities

The Proposal states that a packager is any person or other entity that offers and provides GMPs to borrowers. Proposed § 3500.16(b). The Proposal, however, should clarify that packaging is a primary market function, not open to entities whose charter prevents them from primary mortgage market activities.

E. Conforming the HUD-1 to the GMPA

26. The HUD-1/1A Settlement Statement Should Conform to the GMPA for Ease of Comparison and Should Not Break Out TILA Finance Charges

The Proposal does not require that individual settlement services included in a GMP be itemized in the GMPA. Proposed § 3500.16(d), however, requires that for those loans for which a GMPA is offered, the final HUD-1/1-A settlement statement ("HUD-1") must indicate which third-party settlement services were performed and included in the GMP price, although their individual cost need not be itemized. The "*Instructions for Completing HUD-1 and HUD 1-A Settlement Statements*" indicate that this may be accomplished by putting checkmarks in the appropriate columns, presumably in Section L of the HUD-1, to signify that the services identified in those columns were obtained.

In addition, proposed § 3500.16(d) requires that the packager list separately those closing costs that constitute finance charges under TILA on an addendum to the HUD-1 in order to determine the APR and finance charge disclosures under TILA. HUD has requested comment in Question 20 of the Proposal regarding whether proposed changes to the HUD-1 settlement statement satisfy borrower's rights under TILA and HOEPA.

The CMC does not feel it necessary to itemize those settlement services on the HUD-1 that were not itemized in the GMPA. Therefore, the CMC believes that, despite its common use, the HUD-1 should be revised to conform to the GMPA to make the packaging approach as seamless as possible. We believe that the HUD-1 must track as closely as possible the GMPA so that both the borrower and the lender, as well as persons auditing the loan after closing, will be able to see clearly whether the closing has occurred in accordance with the GMPA.

With respect to the TILA finance charges, while we appreciate the issue, we prefer that breaking out these costs not be made a requirement of the GMP (or of the safe harbor). If a packager chooses to break out those items, it can. They are not useful to an applicant in any event. Applicants neither know nor care which portion of the guaranteed settlement costs are finance charges. Packagers and lenders who need to prepare TILA disclosures know which finance charges are needed to prepare the TILA disclosure.

One-Day Advance Inspection of HUD-1

Under Regulation X, the settlement agent must provide the borrower with the HUD-1 settlement statement one day in advance of settlement. We recommend that this provision be expanded to also require the settlement agent to provide an advance HUD-1 to the packager and the lender (in cases where the lender is not also the packager). This will help the lender assure that no additional charges are being imposed on the borrower beyond the GMP cost amount.

F. <u>Federal Preemption of Inconsistent State Laws</u>

27. HUD Should Affirmatively Express that the Proposed Rule is More Protective of Consumers and/or Competition Than Any Other State Law and Thereby Preempt All Such State Laws That Undermine HUD's Concept of the GMP

In Question 22 of the Proposal, HUD asks for comment on the inconsistencies between state laws and the Proposal, and which types of those state laws merit preemption. We identify below those types of state laws that conflict with, or at least frustrate the purpose of, the Proposal's packaging concept. As discussed below, we believe certain of these laws merit preemption.

In general, a federal law preempts state law if (1) Congress expressly preempts a state law, (2) the state law concerns an area for which there is pervasive federal regulation that "occupies the field," or (3) the federal law and the state law actually conflict. See English v. General Elec. Co., 496 U.S. 72, 78-79 (1990). An actual conflict can be of one of two types: either it is impossible to comply with both the federal law and the state law, or the state law frustrates the Congressional purpose behind the federal law. Duly authorized federal regulations have the same preemptive effect as federal statutes. See New York v. Federal Communications Comm'n, 486 U.S. 57, 64 (1988).

By its own terms, RESPA does not expressly preempt any specific laws or occupy the field of regulation for settlement services or their costs. Section 18 of RESPA states that RESPA expressly does not preempt state laws, except "to the extent that those laws [concerning settlement practices] are inconsistent with any provision of this Act, and then only to the extent of the inconsistency." Moreover, HUD may not determine that a state law is inconsistent if it affords consumers greater protection than RESPA provides itself. Section 8(d)(6) of RESPA further provides, "No provision of State law or regulation that imposes more stringent limitations on affiliated business arrangements shall be construed as being inconsistent with this section."

CMC feels strongly that HUD should preempt certain state laws because their effect frustrates the purpose underlying the GMP safe harbor. The preamble to the Proposal as well as HUD's Economic Analysis make clear that HUD considers facilitating cost negotiations between the packager and its service providers an important goal of the rule.[7] The state laws that frustrate this purpose of the Proposal's packaging approach include:

- State anti-affiliation laws and tie-in restrictions, which would restrict packagers in the amount of settlement service business that they may direct to their affiliates.

[7] "The Secretary has determined, therefore, that effective packaging of settlement services will depend on packagers negotiating lower costs with third party settlement service providers..." (preamble at 55). "The guaranteed packaging approach would remove regulatory barriers that are today preventing market competition from reducing settlement prices. Under current law, a provider's efforts to enter into volume arrangements with settlement service firms may be regarded as illegal and restrictions against mark-ups of third party costs may impede the packaging of services. Under HUD's Proposal, packagers will be able to enter into cost-reducing, volume-discount arrangements, and competition among packagers will pass these lower costs through to borrowers at mortgage settlement." (HUD's Economic Analysis at 5-8).

- State fee restrictions or triggers, including the "points and fees" triggers of state high cost loan laws, which may be deemed to apply to the GMP price as a whole.
- State disclosure laws (including those laws governing conflicting interests, broker disclosures, fees, and terms), which may require packagers to itemize separately the costs of the services included in the package.
- State lock-in/commitment/application fees laws, which often require the lender to provide separate disclosures and/or written agreements with respect to such fees.
- State anti-mark-up laws, which prohibit lenders from marking up third party costs when passing them through to the borrower.
- State kickback and anti-referral fee laws (mini-RESPA laws), which would limit negotiations expressly permitted in the Proposal.
- State advertising restrictions or limitations, which may prevent packagers from being able to compete on a level playing field.
- State laws governing closing practices, which will delay and complicate the implementation of one uniform national package of settlement services.
- State insurance laws prohibiting rebates and "discrimination" in pricing on any grounds.
- State laws requiring borrower choice of service providers, which complicates the concept of packaged services offered at a fixed price because some components of the package may not be used, although paid for, if the borrower selects a different provider.
- State laws requiring the separate disclosure of yield spread premiums so that, for example, such premiums be characterized as "unfair or deceptive."

If these state laws were to remain effective, lenders, brokers and other entities offering GMPs would be prevented from realizing the benefits of the package. Without broad federal preemption the advantages to consumers from the GMP are illusory.

We urge HUD to include in its final rule a determination that state laws that conflict with the GMP, including the above-identified state laws, are preempted. Moreover, HUD should make an express finding in the regulation that the Proposed Rule is more protective of consumers and competition in the marketplace than any other state law or regulation and that preemption applies. Preemption will truly allow "competition [to] substitute[] for regulation," which HUD identifies in its Economic Analysis as a desired effect of providing the GMP option.[8] Such a provision will allow packagers, settlement service providers and others to go forward to implement the rule, relying on Section 19(b) of RESPA, which protects acts done in good faith in conformity with any HUD regulation.

At the same time, we urge HUD to pursue federal legislation that will amplify and confirm the preemption of these state laws. We look forward to working with HUD toward this end.

[8] HUD's Economic Analysis, p. ix.

Part II: Revised Good Faith Estimate

As stated above, we believe that the provision of GMP offers will help consumers shop and exert downward pressure on settlement costs. We urge HUD to waste no time in implementing this aspect of the Proposal to pass these advantages on to consumers immediately.

Under the Proposal, loan originators who do not offer applicants a GMP must provide applicants with the new GFE and comply with the Proposal's new treatment of mortgage broker fees.

Except for the treatment of mortgage broker fees, we urge HUD to postpone action on the GFE. First, the revised GFE raises a host of compliance and operational difficulties that require significant attention before its implementation into the marketplace. Implementing the GMP is a huge enough task. Taking on the mandatory additional project of implementing an entirely restructured GFE, we believe, is too much change at once, particularly as the industry is struggling to implement the Federal Reserve Board's new requirements under the HMDA.

Second, the best and most effective way to gauge the success of the GMP is to measure it against the way business is currently being done. Implementing only the GMP piece of the Proposal will enable consumers to better understand the benefits of the package as compared to the GFE because they will be comparing a new option to an existing option. After measuring the success of the GMP, HUD can decide whether it needs to restructure and enhance the GFE further.

The only change we would suggest be made to the GFE at this point (other than the mortgage broker fee treatment) is to include a statement in the GFE to the effect that the GFE only provides estimates of settlement services and that mortgage entities (packagers) in the industry can provide firm costs through the GMP.

Operational and Compliance Issues with New GFE

Some of the operational and compliance issues that are raised by the revised GFE, as proposed by HUD, include the following:

- The Proposal states that the revised GFE is valid for a minimum of 30 days from the time the packager mails or delivers the GFE to the applicant. The CMC is concerned that if the revised GFE is to remain valid for thirty days, the applicant's information will become stale.
- The preamble to the Proposal states that for the GFE to serve its intended purpose — to apprise applicants with an accurate estimate of settlement costs — tolerance levels must be imposed on certain categories of estimated settlement costs. However, the prescribed tolerance levels leave little latitude for bona fide mistakes made by lenders or for various circumstances that may cause the settlement cost estimates to exceed the tolerance level. Although the Proposal attempts to inject some flexibility in the rigid regulatory standards prescribed above through the qualification of "unforeseeable and extraordinary circumstances," that is far too high a standard to apply given the statutory requirement of an estimate. Moreover, HUD cannot possibly define all those instances in which valid reasons cause an increase in settlement transaction costs. As a result, lenders will likely

encounter situations time and again where tolerance levels have been exceeded due to no fault of their own.

- While HUD has clear authority to issue regulations to carry out the purpose of RESPA, it is questionable whether it has the specific authority to impose, in the context of the GFE, a zero tolerance on any cost category.
- Under the Proposal, if the cost at settlement exceeds the tolerance applicable to the estimate reported on the GFE, absent unforeseeable and extraordinary circumstances, the applicant may withdraw the application and receive a full refund of all loan-related fees and charges. Proposed § 3500.7(d)(2). It is uncertain, however, whether HUD has the specific authority to require such a refund.
- The preamble to the Proposal provides that the rule would require re-disclosure of the revised GFE where there is a counter-offer or where the applicant locks the rate. It appears to be unnecessarily burdensome for the lender to have to send out an additional GFE upon the borrower locking the rate. Without having the redisclosure requirement conditioned on the consumer receiving full underwriting approval, it is possible that there could be three pieces of paper that the originator must send out with respect to one borrower: (i) the initial GFE, (ii) the lock-in GFE, and (iii) if the applicant did not qualify for the initial product applied for, the GFE for a new product that the applicant does qualify for. Such a result is costly for the lender and confusing for the applicant. If the applicant locks, shouldn't the lender be able to provide a disclosure of the locked rate and points, rather than a whole new GFE? In addition, what are the redisclosure requirements where there are applicant-initiated changes that will affect the disclosed information? Will lenders have to redisclose if fees exceed the tolerance due to applicant choice?
- The instructions for the completion of the disclosures on per diem interest indicate the "minimum amount" that the lender will charge be shown, but the revised GFE form indicates that an estimated closing should be used, which creates an inconsistency.
- The escrow deposit will change significantly depending upon the settlement date. How does one accurately estimate that amount?
- Why is owner's title insurance listed as a cost of closing when it is optional?
- Not only does the example of options to pay settlement costs appear to have to be based on the applicant's chosen transaction, it also appears to have to reflect the impact of mortgage insurance in the example.
- The ARM language to be included in the revised GFE is confusing and will not work for all types of ARMs.
- Under the revised GFE, it is unclear whether HUD intended to require lenders to list the names of all required providers on the GFE when the lender has not yet chosen the provider from an approved list of five or more providers.
- For "shoppable" services on the revised GFE Attachment A-1, is the lender supposed to list the name of a suggested provider? Must it do so in order to be able to show that a higher cost for the service is due to borrower choice?

- If the HUD-1 calls line 1101 a settlement or closing fee, why does the revised GFE Attachment A-1 call it a title agent charge?
- The identification of origination charges in revised GFE Section III.A as being the items in the 800 series ignores the fact that not all of the charges in the 800 series are payable to the lender.
- The revised GFE seems to assume that title services will either be all selected by the applicant or all selected by the lender. What if the lender selects some and the applicant selects some?
- Under the revised GFE, shouldn't the lender be able to specify that the loan must close by a reasonable expiration date? Lenders should also not be responsible for honoring the estimates if the applicant is at fault for the failure to close by the specified date.
- The applicant's choice of their hazard insurance coverage could cause the escrow tolerance to be exceeded.
- For shoppable services, may the lender require the applicant to inform the lender of his or her choice of provider within a reasonable time?
- In addition to the collection of rate lock fees, lenders need to be able to charge other fees after the applicant accepts and before the closing.
- Should the description of the rate in the revised GFE be clarified so that the consumer understands that the rate is not locked or guaranteed?
- If a broker does not issue a revised GFE on a timely basis, what is the risk to a wholesale lender who accepts that application?
- How do lenders prevent a settlement agent from adding various junk charges at closing for services that the lender did not require? Aside from a contractual agreement with the settlement agent, what mechanisms could the lender use?

Recommended Changes to Revised GFE

As noted above, we recommend that only the following changes to the GFE be made at this time. These changes will yield benefits for consumers but should not complicate or delay the implementation of the guaranteed mortgage package. These specific changes are discussed in detail below.

28. Mortgage Brokers' Maximum Compensation Should Be Disclosed As a Condition to a Section 8 Exemption

The Proposal fundamentally changes the manner in which compensation to mortgage brokers is recorded and reported to consumers. First, it requires an exact disclosure in the GFE of the total origination charges that will be collected from the applicant and a breakdown of the exact amount of mortgage broker fees. Second, all payments from a lender to a broker based on a borrower's transaction, other than the funding of the loan at par value, must be reported as a lender payment to the borrower. Third, all discount points must be paid in full to the lender.

HUD has requested comment on the particular issue of disclosure of mortgage broker compensation in Question 8 of the Proposal. Of particular importance, the CMC notes that HUD also has requested comment in Question 10 of the Proposal regarding whether a safe harbor exemption should apply to transactions where the mortgage broker signs and contractually commits to its charges on the GFE and in particular, why this exemption is necessary for the industry.

The CMC supports enhanced disclosure of a mortgage broker's compensation so that the applicant is fully aware up front of the maximum amount the broker will receive in the transaction. We believe the best way to achieve this "guarantee" of the mortgage broker's cost, however, is not to recast all compensation (including yield spread premiums) paid to the broker by the lender as compensation to the broker from the borrower paid for with a "credit" from the lender. The difficulty with this approach is that it artificially increases the "points and fees" paid by the borrower for purposes of state high cost loan laws. While there is a good argument that only the "net charge" (the borrower-paid broker compensation less the credit received from the lender) should be treated as "points and fees" under regulations implementing HOEPA, the industry has little assurance of a similar interpretation for purposes of state high cost loan laws. The same issue is raised for FHA loans, but we expect that HUD would be able to clarify that only the borrower's net charge would be counted toward HUD's one percent cap on loan origination fees on these loans. (The VA would have to make a similar clarification.).[9]

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9 HUD is aware that, for FHA-insured loans, in addition to certain specified charges, a mortgagee may not collect from a mortgagor an amount in excess of 1% of the loan's original principal amount. See 24 C.F.R. § 203.27(a)(2). Likewise, for VA-guaranteed loans, in addition to certain specified charges, a lender may charge and a borrower may pay a flat charge not exceeding 1% of the loan amount. See 38 C.F.R. § 36.4312. In addition, the VA Lender's Handbook, at § 8.03, provides that a lender may pay third parties for services, and that, at § 8.04, the VA regulations limit charges "made against or paid by" the borrower, not fees and charges by other parties. Recent court decisions have held that compensation to the broker from the lender in the form of yield spread premiums (YSPs) was not subject to the one-percent caps. In Bjustrom v. Trust One Mortgage the Court rejected the idea that the one-percent cap on origination fees for FHA loans applies to YSPs because the cap only applies to fees collected directly from a borrower, and not to indirect payments of yield spread or servicing release premiums. Similarly, in Geraci v. Homestreet Bank, the Court rejected the argument that Homestreet's payments of a YSP to a broker violated the VA's one-percent cap on loan origination charges, holding that under the plain language of the VA regulation and the VA's own interpretation of the cap, YSPs are not part of the charges included in the one-percent cap because they are lender payments to third parties, not charges paid by the borrower.

We believe a better approach is to require the mortgage broker to disclose its compensation, as well as its role in the transaction, in a "Mortgage Broker Fee Agreement" provided to the borrower with the GFE. Such a disclosure would also result in a safe harbor exemption under Section 8 of RESPA provided the mortgage broker received no more compensation in the transaction than it disclosed This would be similar to the safe harbor exemption for providing a GMP cost amount, but it would apply only to mortgage broker compensation. Applicants who receive this Mortgage Broker Fee Agreement up front and proceed with the transaction would not (and should not) be able to sue the broker or the lender on the grounds that the broker fee was unearned or otherwise in violation of Section 8. This exemption is consistent, we believe, with HUD's new definition of mortgage broker — "a person or entity that renders origination services in a table funding or intermediary transaction...." Such definition recognizes brokers for what they are and appears to move away from a requirement that brokers must perform some set number of identified settlement services to justify their fee. If the broker fully discloses and guarantees its maximum compensation and no more than that amount is collected at settlement, that compensation should be protected from claims under Section 8.

Amounts received by the mortgage broker in excess of the disclosed maximum would not benefit from the safe harbor exemption and may subject the mortgage broker to a breach of contract claim.

This recommendation will achieve HUD's objective of better informing the applicant of the broker's compensation early in the transaction and removing the ability of mortgage brokers to increase their compensation through subsequent changes in the interest rate or discount points. Once the maximum compensation is disclosed, the broker may not increase that compensation by adjusting the interest rate on the loan. Such disclosure also will inform the applicant of the broker's role in the transaction and the options for paying the mortgage broker compensation - both of which items are included in the Mortgage Broker Fee Agreement.

We also recommend that, to achieve as much uniformity as possible, HUD make a determination that the Mortgage Broker Fee Agreement, which discloses the mortgage broker's role and fees, when given, is more protective of consumers than inconsistent state law mortgage broker disclosure forms or agreements, such that those state forms would be preempted when the federal form is used.

In addition to regulatory language implementing this recommendation at Tab 3, we have included a form of "Mortgage Broker Fee Agreement" at Tab 6.

29. The Revised GFE Should Include a Statement That Clarifies to Consumers That the GFE Provides Estimates and Is Not a Guarantee of Settlement Costs

The CMC also recommends that there should be an additional disclosure provided to the consumer upfront to clarify that the GFE is a "good faith" estimate, and not a guarantee of settlement costs like the GMP. Such a disclosure should minimize the risk of unwarranted unfair and deceptive acts and practices claims.

Part III: Other Changes

30. Payments for Advertising under Section 8 Should Be Clarified to Ensure That They Are Permissible under Section 8.

We urge HUD to take this opportunity to clarify the treatment of payments for advertising under Section 8 of RESPA. It is increasingly common for loan originators and other service providers to enter into agreements for advertising and other general promotion on the Internet or in other media. This type of general promotion arguably should not constitute a referral because it is not directed to a particular person, but is understood to be widely disseminated to large segments of the public.

In our view there is no reason to treat payments for such advertising and promotional activity as impermissible under Section 8.

Thus, we recommend that HUD amend §3500.14(g) of Regulation X to provide that RESPA permits:

"a payment made or received by any person in connection with an advertisement of settlement services. Any link, banner, brochure or other promotional message, whether communicated on an electronic medium or otherwise, whose characterization as an advertisement is unclear shall be deemed an advertisement for purposes of this section if its accompanied by a clear and conspicuous notice indicating that it is an advertisement."

This clarification will permit advertising arrangements that are common and cost-effective in other industries to be engaged in the residential real estate and home mortgage industry. Consumers are protected because if it is unclear whether a message is an advertisement, the provider of the message will label it an advertisement in a clear and conspicuous manner.

Part IV: Responses To HUD's Questions For Commenters

We address below the questions presented by HUD with respect to the proposed GMP, revised GFE and the disclosure of mortgage broker compensation. The questions are numbered as they are in the Proposed Rule. In addition to responding to HUD's question directly, we also provide a cross-reference to the body of the letter where we have addressed the relevant issue in greater detail.

A. The New Good Faith Estimate (GFE) Requirements (#1-10, #29-30)

We do not address each HUD question regarding the revised GFE requirements as proposed in the rule. As noted above, we believe that HUD should not adopt any sweeping changes to the GFE at this time, with the exception of the enhanced disclosure of mortgage broker compensation, coupled with a Section 8 exemption. We firmly believe that HUD is on the right track with the Proposal, but are of the opinion that HUD will be able to implement the proposed GMP and accomplish its stated objectives more quickly and effectively if its refrains from substantially revising the existing GFE at the same time. From a training, compliance and systems changes standpoint, the Proposal is of such a magnitude that it must be considered and implemented in stages. The GMP should be implemented as soon as possible. The structural changes to the GFE, with the exception of the treatment of mortgage broker compensation, should be put off until the HUD and the industry have implemented the GMP and have, with the perspective of how readily the GMP is embraced, gauged the changes necessary for the GFE.

B. Guaranteed Mortgage Package Agreements (#11-28)

11. Is a safe harbor along the lines proposed in Section III.C.(1) of this rule necessary to allow lump sum packages of settlement services to become available to borrowers? Would the proposed clarification by HUD that discounts may be arranged, if passed on to borrowers and not marked up, suffice to make packages available to borrowers? Would a rule change to approve volume discounts and/or mark-ups when a package is involved suffice? Would it suffice to trim the disclosure requirements for packaging and offer the option of providing a streamlined GFE to those who packaged?

The CMC has long held the view that a Section 8 safe harbor exemption is necessary to allow packagers to negotiate freely with settlement service providers for lower costs, which are then passed on to consumers. The GMP not only provides upfront information about certain closing costs, it also provides consumers with a measure of certainty about the cost of their loan, which makes comparison shopping easier and more fruitful. A narrow exemption allowing for volume discounts and/or mark-ups is inappropriate for this rule because it unnecessarily constrains the range of possible packager/vendor negotiated arrangements and injects needless uncertainty for any variant from a simple agreement that fits the express, narrow exemption. Without a safe harbor, packagers will not have the incentive to enter into such arrangements for fear of unintentionally violating Section 8 and being subject to increased risk of litigation. We note, however, that the scope of the safe harbor exemption should also provide for a cure provision. We discuss the safe harbor exemption and various aspects of it under item 21.

12. As proposed in Section III.C.(6) is the scope of the safe harbor appropriately bounded in applying to all packagers and participants in packages? The safe harbor also currently does not apply to referrals to the package. Should there also be a bar against part time employees of other providers working for the package to steer business? How should the safe harbor apply to affiliated business arrangements to protect borrowers from steering?

We believe the safe harbor is appropriately bounded in applying to all packagers and participants in packages. We also believe that the safe harbor exemption should be conditioned solely on the borrower paying no more for packaged settlement services than the amount of the guaranteed settlement costs set forth in the GMPA. HUD should also make clear that the safe harbor exemption and the arrangements covered by the exemption may not be used to challenge referrals to service providers in connection with GFE loans. In addition, HUD should not be concerned about additional provisions to the Proposal regarding affiliated business arrangements to protect consumers from "steering." It should not matter whether packagers negotiate volume-discount or affiliated business arrangements, or whether part-time employees or other providers generate business, so long as in the end, the packager offers the consumer a GMP at a guaranteed lump sum cost. The freedom for packagers to negotiate freely to obtain the lowest costs, which are then passed onto the consumer, is the precise point of the GMP concept. These issues are addressed in greater detail under item 22.

13. As proposed in Section III.C(5), to qualify for the safe harbor, the packager must include an interest rate guarantee with a means of assuring that when the rate floats, it reflects changes in the cost of funds not an increase in originator compensation. For this purpose, the rule suggests tying the rate to an observable index or other appropriate means. What other means could assure borrowers that the rate of a lender was not simply being increased to increase origination profits? For example, would a lender's commitment to constantly make rates public on a web site be a useful control? If an index is the best approach, how should it be set? If an index approach is approved, should each lender be allowed to pick its own observable index?

HUD's requirement that the consumer be able to track a floating interest rate should be satisfied by the packager making its rates constantly public on a website or other widely accessible medium, such as the telephone. The alternative requirement that the interest rate must float according to an observable and verifiable index is highly problematic and does not take into account numerous legitimate pricing concerns. We address this issue further under item 8.

14. As discussed in the preamble to the rule in Section III.C(5), if an observable index or other appropriate means of protecting borrowers from increases in lender compensation when the borrower floats in a guaranteed packaging approach is not practical, should HUD provide a packaging safe harbor only for mortgage brokers? Such a mortgage broker safe harbor would require disclosing the lender credit to the borrower in broker guaranteed packages. The theory for the safe harbor would be that any amounts in indirect fees could be credited to borrowers taking away any incentive for an increase in rates to increase compensation. Should this be offered in any event?

No, the safe harbor exemption should not be available only for mortgage brokers. As noted in response to HUD Question #13, providing interest rates on a packager's website or making them available by telephone should satisfy HUD's concerns that an applicant who locks in a rate is treated similarly with all other similarly-situated applicants.

15. As proposed in Section III.C(6), under the rule, mortgages with total fees or a rate covered by the Home Ownership and Equity Protection Act (HOEPA) would be subject to the new GFE disclosure requirements; however, HOEPA loans would not qualify for the guaranteed package safe harbor. Is this exclusion appropriate considering, on the one

hand, that packaging promises borrowers a simpler way to shop and make transactions more transparent? On the other hand, the safe harbor could be provided for a loan that has very high rate and/or fees and may be predatory. The proposal also says that during the rulemaking other limitations may be established to exclude high cost and/or loans with predatory features from the packaging provisions. HUD invites comments on whether HOEPA loans, any other loans, or features of loans should be included or excluded from the safe harbor and why.

We believe that excluding HOEPA loans from the safe harbor is inappropriate because doing so will prevent HOEPA loan consumers from sharing in the reduced costs and better disclosures the GMP will afford them. Moreover, the most effective measure against abusive lending practices is to provide consumers with clear, upfront relevant settlement cost information that enables them to comparison shop mortgage loans. We address these issues further under item 20.

16. As proposed in Section III.C(3), the GMPA provides that the offer must be open to the borrower for at least 30 days from when the document is delivered or mailed to the borrower. Is this an appropriate minimum time period to ensure that the borrower has an adequate opportunity to shop?

The GMP offer should be open for a minimum of ten days, not thirty, to avoid having the information provided become stale. We believe that ten calendar days is ample time for a consumer to shop the GMP cost. We do suggest, however, that once the borrower accepts the GMPA, the packager should be able (as loan originators do today) to require that settlement occur by a certain date for the offer to remain effective. We discuss this issue in further detail under item 7.

17. As proposed in Section III.C(4), the rule currently provides that the Guaranteed Mortgage Package agreement must indicate that certain reports such as the appraisal, credit report, and pest inspection are available to the borrower upon the borrower's request. Also, packagers may decide to forego such reports or services (i.e. lender's title insurance) and must inform the borrower that such reports or services are not anticipated to be included in the package price. Are these adequate protections for the borrower? HUD is aware that other laws such as Regulation B (ECOA) provide certain rights to borrowers with respect to obtaining some of these reports. In order to qualify for the safe harbor HUD has created additional reporting requirements. Are these additional reporting requirements appropriate?

Except for the pest inspection report, which should not be burdensome to provide, it is unnecessary to require that these reports be made available upon request. Rather, HUD can still adhere to the packaging concept by requiring that the packager inform the consumer that he or she may inquire whether the packager has obtained these reports and to leave it to the packager's discretion whether to provide them to the consumer. We discuss this issue further under item 18.

18. Should additional consumer protections be established for packaging? For example, should additional qualifications be established for "packagers" to ensure that borrowers are protected against non-performance including the unavailability of a mortgage that

could result in a borrower ''losing'' a house? For example, should there be a requirement that a packager must have sufficient financial resources to credibly back the guarantee? Is it necessary to require a lender signature on the GMPA to ensure that the borrower receives the loan at the time of settlement? How can the borrower's interests be protected without unduly burdening the process or unduly limiting the universe of packagers?

We do not believe that it is necessary to codify additional consumer protections for packaging because adequate safeguards are already in place. For example, consumers will be adequately protected due to state mortgage broker and mortgage banker licensing laws that impose net worth requirements. A non-loan originator packager such as a title company or a real estate company will need to make arrangements with such a licensed entity or exempt lending institution. We recommend, however, that HUD require that non-lender packagers certify to the consumer in the GMPA that it has arrangements with one or more lenders to provide loans to consumers who accept the GMPA and are finally approved for financing. In light of current practices where mortgage brokers routinely communicate exclusively with the consumer until settlement, we also believe that it is not necessary to require a lender signature on the GMPA to ensure that the applicant receives the loan at the time of settlement. This issue is addressed in greater detail under item 24.

19. Consistent with the HUD-Fed Report, the rule proposes that certain charges, such as hazard insurance and reserves, are outside the package as other or optional costs. Is this the right approach or should these charges be disclosed as the minimum amounts required by the lender and required to be inside the package? Would the latter better serve the objective of establishing a single figure for the borrower to shop with?

Escrow reserves for taxes and insurance should remain outside of the package. Consumers do not shop based on these amounts and RESPA's escrow rules assure that permissible escrow cushions are not exceeded. In addition, while we strongly agree with HUD's approach to include as many services as possible in the package, we nonetheless believe that including in the package certain other costs, such as up front mortgage and flood insurance premiums, which cannot be known until after the GMP is offered, is more detrimental to the overall packaging concept than excluding them. Those costs that we feel should be excluded or included in the GMP are discussed further under items 13-17.

20. The rule proposes in Section III.C (3), that under Guaranteed Mortgage Packaging, the HUD–1 will list the settlement services in the package but not the specific charges for each service. Certain third party charges are excluded from the calculation of the finance charge and the APR under TILA and HOEPA. Commenters are invited to express their views on whether the approach in the rule satisfies or whether alternative approaches to cost disclosures should be established to ensure consumers' rights under TILA and HOEPA are protected while facilitating packaging. More broadly, commenters are invited to provide their views on means of better coordinating RESPA and TILA disclosures.

First, we believe that TILA finance charges should not be required to be broken out as a RESPA requirement. If they are required to be broken out, they should be shown as a sum total of charges, without individual itemization. Similarly, under HOEPA, packagers will determine what portion of the package is properly characterized as "points and fees." Under our recommendations above, the discount points would be outside of the GMP price, and thus easy to calculate, and treated separately as a component of the interest price of the loan. In the short term, the packager should be able to certify that the portion of the package costs amount that represents points and fees is a particular number. In the longer term, we believe that the Federal Reserve Board and HUD should work together toward establishing a new "points and fees" threshold for triggering HOEPA coverage in a packaged loan scenario. Second, until RESPA and TILA are harmonized by legislation, we are very concerned about the confusion that may be caused by HUD importing TILA disclosures into the GMPA. We recommend that, except for straightforward information that informs the applicant whether his or her loan has a prepayment penalty, balloon payment, or adjustable rate terms, the information contained in the initial TILA disclosure not be duplicated in the GMPA because this will be costly to packagers and confusing to consumers. These issues are addressed further under item 3.

21. Commenters are asked to provide their views on how the rules should treat mortgage insurance? The rule proposes in Section III.C(3), that the guaranteed package would include any mortgage insurance premiums in the APR and up-front costs of mortgage insurance in the guaranteed package. ''Other Required Costs'' would include reserves for mortgage insurance premiums. However, because the packager will not have an appraisal at the time the GMPA is provided, the packager may not have firm information to provide a definite figure. Another possibility is to exclude mortgage insurance from the package but notify the borrower that mortgage insurance may be an ''Other Required Costs'' and present the borrower an estimate subject to a tolerance, if mortgage insurance is necessary. This approach would exclude a major charge from the package. HUD recognizes that there are state laws that prohibit rebates or any splitting of commissions for mortgage insurance. How, if at all, should this impact the decision to include mortgage insurance in packages of settlement services?

The GMP price should not include mortgage insurance because it is a cost that is difficult to ascertain with certainty upfront and, therefore, frustrates HUD's purpose of providing a firm GMP price to the consumer early in the shopping process. In addition, although mortgage insurance may have been a major settlement cost in the past, it is no longer in the vast majority of cases because most private mortgage insurance policies today are monthly-pay policies with little, if any, upfront premium. We recommend, however, that in order to provide the consumer with the most useful information possible at application, the packager should provide the applicant with a mortgage insurance disclosure[s] that contains an estimate of the cost of the upfront mortgage insurance premium. This issue is discussed further under item 13.

22. To what extent, if any, do inconsistencies currently exist, or would they exist upon promulgation of the proposed rule between State laws and RESPA? Specifically, what types of State laws result in such inconsistencies and merit preemption? What, if any, provisions of the proposal should be revised to facilitate any necessary preemption?

Many inconsistencies exist between the proposal and state laws relating to disclosures, mini-RESPA laws, fee and interest rate restrictions and tie-in restrictions, to name a few. Many of these state laws merit preemption because their effect frustrates the purpose underlying the GMP safe harbor. We recommend that HUD make an express finding that the proposed rule is more protective of consumers and competition in the marketplace than state laws or regulations that conflict with the GMP. Preemption of certain state laws is discussed further under item 27.

23. The rule proposes that the GFE and the GMPA be given subject to appraisal and underwriting. How should the final rule address the matter of loan rejection or threatened rejection as a means of allowing the originator to change the GFE or GMPA to simply earn a higher profit?

If the applicant accepts a GMP offer and upon full underwriting the packager determines that the applicant does not qualify at the preliminary rate offered in the GMP, the packager must either counter offer or issue a notice of adverse action. If a counter offer is given, a new GMP offer would be given, re-initiating the shopping process.

24. To what extent, if any, should direct loan programs such as those provided by the Rural Housing Service of the Department of Agriculture be treated differently under the new regulatory requirements proposed by this rule?

To the extent that such programs compete with programs offered by private lenders, the rules should be the same.

25. As proposed, the GFE and GMPA currently contain sections for loan originators and packagers to indicate the specific loan terms for adjustable rate mortgages, prepayment penalties, and balloon payments. Are these appropriate loan terms to include on these forms, and what, if any, other mortgage terms or conditions should be listed on the forms?

We do not believe that these are appropriate loan terms to include on the GMPA because including these terms is merely duplicative of information already contained in the TILA disclosures and, therefore, increases costs to packagers and confuses consumers. These issues are addressed in further detail under item 3.

26. What are the arguments for or against limiting the proposed rule to purchase money, first and second lien, and refinancing loans as opposed to offering it to home equity, reverse mortgage and other transactions? Should there be any additional requirements for so-called B, C, and D loans?

We believe that the GMP should apply to home equity lines of credit to allow consumers to better compare prices and shop for the best deal available to them. This issue is addressed further under item 23. There should be no additional requirements for B, C and D loans.

27. As proposed, the Guaranteed Mortgage Package includes one fee for settlement services required to complete a mortgage loan. The fee for the package will include loan

origination fees, typically referred to as "points." As points are generally deductible under IRS rules, comments are invited as to how to determine which portion of the package prices should be deemed to constitute points.

We recommend that discount points not be included in the GMP cost amount, but be disclosed together with the interest rate on the first page of the GMPA as the price of the loan that the applicant selected and the packager is offering, conditioned upon final underwriting. Excluding discount points from the package price will easily enable the consumer to know what points are deductible for tax purposes.

28. To what extent do the proposed changes to the definition of application in Section III.B (2)a, and requirements for delivery of the GFE impact other federal disclosure requirements, such as those mandated by the Truth in Lending Act? How can the disclosure objectives of the proposed rule be harmonized with such other disclosure requirements?

We recommend that the application, as defined in the Proposal, be bifurcated into two components: a "Shopping Application," which consists of information submitted in anticipation of a GMP offer (or a GFE in non-GMP transactions), and a "Final Application," which consists of information submitted, upon acceptance of the GMPA (or GFE) in anticipation of a credit decision. Shopping Applications should trigger disclosures under Regulations X and Y to allow shopping to occur, but should be treated as a "pre-qualification" for purposes of Regulations B and C. Creditors should not be forced to treat every submission for a GMP offer as an application for Regulation B and C purposes because to do so will create severe customer relations problems and skewed HMDA reporting. These issues are addressed further under item 10.

We look forward to working with the Department on these important issues as it moves toward finalizing a regulation that, if structured appropriately, will improve shopping and lower costs for consumers.

Sincerely,

Anne C. Canfield
Executive Director

Tab 1

Proposal to Address Predatory Lending

The Consumer Mortgage Coalition ("CMC") believes that to find a fair and practical solution to eliminate fraudulent and abusive mortgage origination practices that have victimized consumers, the focus should be on reforming the origination process so that consumers can effectively shop for the most appropriate loan. In short, empower consumers to use the market and let market competition serve consumers.

To accomplish this we first need mortgage reform to simplify the mortgage shopping process and to encourage more borrowers, particularly those with blemished credit, to comparison shop for loans. Second, we need to institute a widespread public awareness and education campaign, which could include government-sanctioned tools to help consumers understand the loan process and to compare loans. Third, we need to make financial counseling widely available to potential borrowers to help them make wise loan decisions. Fourth, we should make the licensing violations of mortgage brokers and lenders available to the public so that borrowers can be forewarned when dealing with these entities. Fifth, we need competitive underwriting systems that will provide the greatest opportunities for borrowers with some blemished credit to obtain the best loan. Finally, to the extent federal legislation is pursued, we need uniform rules for the whole country that reflects the national nature of this business. Each of these prescriptions is addressed below.

THE IMPORTANCE OF MORTGAGE REFORM

The CMC has worked toward reforming the mortgage origination process since its inception. The mortgage industry is on the verge of tremendous advances that will provide great benefits to consumers *if* we can secure appropriate regulatory relief that allows technology and market competition to improve the delivery of mortgages to consumers at lower costs.

Regulatory Relief #1: The E-Sign Act

The principal regulatory relief necessary to unleash far-reaching technological advances has already occurred. The Electronic Signatures in Global and National Commerce Act ("E-Sign Act"), enacted two years ago, ensured the legal effect of electronic signatures, contracts, and disclosures. The CMC played a leading role in securing the passage of the E-Sign Act, and particularly the provisions that allow consumer disclosures to be provided on-line and mortgage loans to be effectively transferred electronically. This law has paved the way for the full "electronification" of obtaining a mortgage, from application to closing to recording to sale in the secondary market.

This electronification of mortgages should significantly lower interest rate costs by reducing the hedging costs associated with the time gap between the application and funding of a loan. The reason today that mortgage loans, and particularly first mortgage loans, are not like other consumer goods that borrowers can simply buy off the shelf at a listed, unchanging price is the time gap between the time a borrower applies for a loan and the time that loan is actually closed and funded. When applications come in, lenders must reserve money from the capital markets to fund the loans at a future date, often at specified prices. This involves hedging costs. The effects of the E-Sign Act, together with advances in automated underwriting and property valuation, should shorten that time gap, reducing hedging costs considerably.

Regulatory Relief #2: RESPA Reform

The second regulatory relief that is necessary to allow market competition to bring maximum benefits to consumers in the form of lower settlement costs is RESPA reform. This reform has four objectives: (i) to streamline and simplify the disclosures provided to borrowers so that they will have better and more certain information with which to make wise credit choices; (ii) to lower settlement costs by removing the regulatory barriers that insulate these costs from the effects of market competition; (iii) to reduce abusive lending practices; and (iv) to ease the burden of compliance by adding much-needed certainty into RESPA's and other related regulatory requirements, which should reduce the continual onslaught of class action litigation that is spawned by ambiguous rules.

The CMC has been working to accomplish these objectives since 1996 when, working with other mortgage trade associations, we developed a series of proposals to bring to Capitol Hill for consideration. At that time, members of Congress directed us to work with a broad group of consumer advocates and representatives of other banking, lending, title, real estate and other settlement services industries to reach consensus on broad-based mortgage reform, including substantive consumer protections. This resulted in the formation of the Mortgage Reform Working Group (MRWG), which, despite approximately two years' continuous meetings and negotiations, was unable to reach consensus among all the varying interests. Although the MRWG process yielded greater understanding of the concerns of divergent interest groups, at the end of the day it remains clear that the ultimate leadership for meaningful mortgage reform must come, not from the industry or the consumer advocacy groups, but from our government.

Much time has passed since the MRWG process ended, with no regulatory changes. That means that mortgage loans today continue to be governed by a disclosure scheme put in place over 25 years ago, at a time very different from our own. Congress gave HUD the authority under RESPA to create exemptions for classes of transactions that would effectuate the Act's purposes, including the purpose of reducing unnecessary settlement costs. As discussed below, the reforms we have recommended, which are consistent with those HUD has proposed, would do exactly that.

The Value of Guaranteeing Settlement Costs

Our recommended reforms include the disclosure of a guaranteed, bundled closing cost amount. Contrary to the view, expressed by some consumer advocates, that a guaranty of settlement costs would provide little of value to the consumer, unless it also included a binding guaranty of the interest rate on the loan, we believe the guaranty of settlement costs addresses consumers' core complaint with the mortgage origination process - being "surprised" at closing by high costs and fees that either greatly exceed the cost or fee estimated on the good faith estimate or were not previously disclosed at all. Unexpected, high closing fees often leave borrowers in a no-win position at the closing table. Most borrowers will not walk away from the closing because they are too far along to start the process over. Some need the loan to consummate their purchase of a new home. Others may need the money to cover other expenses, like home repairs or college costs, which cannot be delayed. Whatever the reason, because of the pressures to close the transaction and get the loan, they often have no real choice but to pay the higher fees.

A guaranty of settlement costs will end this problem. Borrowers will know for certain early in the process what fees they will pay at closing. Most importantly, they will also be able to shop for loans based on these costs. Although we have recommended that the guaranteed closing costs would not be required to be disclosed until the application is taken (or within three days thereafter), lenders and brokers offering guaranteed closing cost packages will certainly promote these guaranteed costs during inquiries from potential borrowers. Any discrepancy between such a promotion and the immediately following application disclosure will be readily apparent for borrowers to question and possibly subject to charges of unfair and deceptive practices.

In addition, with an exemption for RESPA's prohibitions for this guaranty, lenders will be able to use their purchasing power to reduce these costs (by negotiating and passing on volume discounts), helping to remove one of the major impediments - high closing costs - faced by first-time homebuyers seeking to close their first mortgage loan. This is a very significant benefit to consumers and a vast improvement over the current disclosure process.

Finally, this reform proposal provides simplification. Consumers report being overwhelmed by the complexity of the home lending transaction. This change creates simplicity - allowing consumers to better focus on what is important. For these reasons it is simply not true to say that this guaranty is of little value to the consumer without a guaranty of the interest rate.

The Benefits of Guaranteeing the Interest Rate Do Not Justify the Costs

It is worth our examining the merits of the position of some consumer advocates that, in addition to guaranteeing closing costs, lenders should be required to guarantee the interest rate for all consumers making inquiries about a loan. As noted in our comments, we do not regard HUD's proposal to include an interest rate guarantee. It is a conditional rate that should be labeled as such.

We are opposed to a requirement for a true interest rate guaranty because, for the reasons outlined below, the benefits of such a guaranty simply do not justify its costs. It should be noted that most lenders currently offer the consumer the ability to lock-in a rate at application. If the consumer qualifies for the loan product for which they applied, the consumer will get that loan at the rate they locked.

First, for loan shopping purposes, it makes sense to guarantee only those items that are uncertain, elusive, subject to deception, hidden or partially hidden, and not subject to competition. Closing costs fit this description, not interest rates. Borrowers today shop for loans based on interest rates. The first question they ask when they call a lender is "what are your rates?" For this reason, market competition is very much alive and well in the offering of rates for comparison. Moreover, while rates sometimes change, even during the same day, it is not a hidden process. For example, if a borrower calls up a lender to get its latest rates, then shops around to compare those rates, then calls the original lender back, any change in the lender's rate will be very clear. This change may be based on pricing changes in the capital markets or on the lender's pricing strategy at the moment to attract more of a certain type of loan product, for example, to fill a commitment to an investor. But there is no lack of information. There is no question about what the rate is. There have been very few complaints about this process of offering interest rates in the mortgage process, something that cannot be said of the process of charging closing costs.

Second, as noted above, with the E-Sign Act and advances in technology, the time gap between application and funding can be expected to be reduced, resulting in lower interest rates. We are greatly concerned that requiring a guaranty of interest rate at the inquiry stage will have an opposite effect - a lengthening of this time gap, depending upon how long the rate must be guaranteed. At the very least, the infrastructure necessary to, in effect, lock in a rate for every borrower inquiry will require a massive implementation and maintenance system, considering that the number of borrower inquiries may greatly exceed the number of actual applications.

Finally, as noted earlier, there is an existing procedure for guaranteeing rates in the mortgage shopping process. If the borrower wants to be sure the rate does not change, he or she may simply apply and lock in the rate.

On the other hand, the costs of guaranteeing the interest rate for all borrower inquiries would be extreme. There is no doubt that requiring lenders to guaranty the interest rate would significantly increase rates to all consumers across the board. Although the industry did not commission a full-fledged economic study of these costs during the MRWG process, we did explore with hedging analysts the potential effect of these costs. All indicated that rates would increase significantly, depending upon the length of the guaranty, with one indicating that guaranteeing the interest rate for all shopping inquiries from potential borrowers could result in an increase in interest rates of ½ percent or more per day.

We believe RESPA reform is an integral part of a practical solution to abusive brokerage and lending practices. As noted above, guaranteeing settlement costs early in the transaction provides more certain cost information for borrowers to comparison shop. It also eliminates abuses where the consumer is surprised by unknown fees at closing, which is among the greatest source of complaints by borrowers in the mortgage industry today. With the pending "electronification" of mortgages, which will shorten the time from application to funding and thus reduce hedging costs, and the borrower's ability to lock in interest rates at application, we believe interest rates will also be lowered for all consumers.

We recognize, however, that while RESPA reform can play a key role in combating predatory lending, it is not the whole solution. In addition to reform of the mortgage process, and an appropriate mortgage broker disclosure, the CMC believes that the following steps should be pursued immediately by the relevant government agencies to curb predatory lending practices.

A COMPREHENSIVE PUBLIC AWARENESS AND EDUCATION CAMPAIGN

Federal policymakers should implement an ongoing, nationwide public service campaign to advise consumers, particularly the more vulnerable, of the basics of obtaining appropriate loans. Public service announcements could be made on radio and television, and articles and notices could be run in local newspapers and selected publications. Given that people's homes are at stake, these messages should be every bit as pervasive as the anti-smoking public interest announcements that have frequently appeared in the media in the last several years. This campaign should highlight the importance of obtaining the advice of an independent third party before signing any loan agreements.

COUNSELING

Once alerted, consumers will need to be able to avail themselves of counseling services from unbiased sources. Those sources can always include family and friends and industry participants. In addition, however, a nationwide network should be put in place to ensure that all consumers can easily access advice and counseling to help them determine the loan product that best fits their financial needs. A public awareness infrastructure could be built out that would include 1-800 numbers with independent counselors, using sophisticated computer software, to help consumers talk through the loan product they are considering. In addition, programs could be developed with community organizations and other organizations serving senior citizens to provide on-site counseling assistance at local senior and community centers and churches. HUD's 800 number for counseling could also be listed on required mortgage disclosures as an initial step to increase awareness of available counseling.

The *Joint Report on RESPA and Truth in Lending Act* issued in 1998 by HUD and the Board of Governors of the Federal Reserve System (the "Board") recommended that the government develop "smart" computer programs to help consumers determine the loan product that best meets their individual needs. Mortgage calculators or "smart" computer programs are now available online. Since these computer programs were already developed by the private sector and are widely available, a process where the Board reviews and certifies those programs that it determines are effective in enabling consumers to comparison shop among loans would lend credibility to, and increase the use of, these programs.

A NATIONWIDE LICENSING REGISTRY

Consumers need to be able to evaluate the competency and integrity of the mortgage originators with whom they are dealing. For this reason, a nationwide licensing registry should be established on which state regulators could detail consumer complaints, licensing suspensions and revocations that would be accessible to consumers. The bonding requirements for mortgage brokers should also be increased so that claims against predatory mortgage brokers are more viable.

COMPETITIVE AUTOMATED UNDERWRITING SYSTEMS

Enhanced competition serves borrowers, both in terms of lower costs and greater choices. While we have put forth a proposal to increase competition for a loan's costs, we also need greater competition in the underwriting systems that are used to underwrite the vast majority of mortgage loans in this country, which will lead to greater choices. The problem is that two automated underwriting systems ("AUS") -- Freddie Mac's Loan Prospector and Fannie Mae's Desktop Underwriter - dominate the market.

The development of AUS and automated property evaluation systems is a significant advance that, as noted above, is part of the "electronification" of the mortgage process that has benefited and will continue to benefit consumers. They can shorten the time from application for a mortgage to approval from weeks to minutes, facilitate accuracy in mortgage documentation, and reduce consumers' costs. However, the dominant use of the GSEs' AUS has raised concerns about whether the GSEs are limiting access to the mortgage market for many borrowers because these AUS are perceived to allow lenders less flexibility in considering compensating factors or alternative credit history (e.g., utility bills or rental payments) that would permit disadvantaged borrowers to qualify for conforming loans.

HUD has been concerned about these issues for several years and commissioned the Urban Institute to study them. That study concluded that the GSEs have made some progress in adding flexibility to their underwriting guidelines, but that "[t]he GSEs' guidelines disqualify a disproportionate share of lower income and minority borrowers. Primary lenders are making more aggressive efforts to serve such borrowers by offering loan products that are more flexible than the GSEs' guidelines." Even without a study, however, it simply stands to reason that multiple underwriting systems that provide alternative and more flexible standards are better for consumers than just two. More competition, more choices.

Benefits for Minority Borrowers

We note that among those who would benefit from multiple underwriting systems are minority borrowers who do not meet the standards of the GSEs' AUS, but would meet a more flexible, alternative AUS. Competition, which is colorblind by nature, helps overcome potential disadvantages of using limited underwriting systems.

ULTIMATE NEED FOR UNIFORM, NATIONAL RULES

Although real estate has traditionally been regarded as a state law concern, it is clear that mortgage lending is a national industry where it is routine for lenders to lend in multiple states, loans and loan servicing rights to be transferred across state lines, and pools of loans from around the country to be assembled and placed in securities which are sold on the national capital markets. We believe that such a national industry should ultimately have the same, uniform rules that apply to all. Consumers should have the same protections, whether they are in Maine or California, and lenders and servicers should operate on the same, level playing field of regulation across the nation. As you know, state and local governments across the country are enacting or considering legislation that would implement different standards and impose varying levels of prohibitions on lenders. This vastly increases lenders' costs of compliance, which are ultimately passed on to consumers through higher mortgage rates. We hope that any federal legislation that is considered addresses these concerns by preempting state and local predatory lending laws while providing the same substantive protections from abusive lending to all consumers.

Tab 2

Discount Points Options Examples

January 1 - Date of GMPA – Pricing for Consumers Applying for $200,000 Loan on that Date

Rate	Points	Closing Costs	Total of Points and Closing Costs
6.25	1	2,000	4,000
6.375	.5	2,000	3,000
6.500	0	2,000	2,000
6.625	.5 credit	2,000	1,000

January 10 - Pricing for $200,000 Loan for Consumers Applying on that Date
(Points Decrease by .25 and Closing Costs Increase by $100 from January 1)

Rate	Points	Closing Costs	Total of Points and Closing Costs
6.25	.75	2,100	3,600
6.375	.25	2,100	2,600
6.500	.25 credit	2,100	1,600
6.625	.75 credit	2,100	600

January 20 - Pricing for $200,000 Loan for Consumers Applying on that Date
(Rates Increased by .125% and Closing Costs Increase by $100 from January 1)

Rate	Points	Closing Costs	Total of Points and Closing Costs
6.375	1	2,100	4,100
6.500	.5	2,100	3,100
6.625	0	2,100	2,100
6.875	.5 credit	2,100	1,100

Assume the GMPA issued on January 1 reflects the 6.5% rate. There are two disclosure options:

Option A (CMC's Preferred Option):

Rate	Points	Closing Costs	Total of Points and Closing Costs
6.500	0	2,000	2,000

Option B (Proposal's Option):

Rate	Points	Closing Costs	Total of Points and Closing Costs
6.500	Undisclosed	Undisclosed	2,000

If Consumer Accepts the GMPA and Rate is Established on January 10:

Option A: The applicant could choose any of the rate/discount point combinations. For example, the applicant could choose the 6.375% rate and pay .25% in discount points ($2,500 in total costs when adding the $500 in discount points to the $2,000 closing costs) or the 6.500% rate and receive a .25% credit ($1,500 in total costs when subtracting the discount credit ($500) from the $2,000 closing costs).

Option B: The applicant's rate would be 6.500% and the borrower would pay $2,000, which is $500 more than under Option A for the same rate.

If Consumer Accepts the GMPA and Rate is Established on January 20:

Option A: Again, the applicant could choose any of the rate/discount point combinations, including a 6.625% rate with 0 discount points, in which case the total costs would be $2,000.

Option B: The borrower would pay $2,000, but it is not clear if the rate should be 6.625% or 6.875% since discount points and closing costs are melded together under this option.

Tab 3

CMC Recommended Changes
To HUD's Proposed Regulation

[[49158]]

VI. Rule Language

List of Subjects in 24 CFR part 3500

Consumer protection, Condominiums, Housing, Mortgagees, Mortgage servicing, Reporting, and recordkeeping requirements.

Accordingly, for the reasons set out in the preamble, part 3500 of title 24 of the Code of Federal Regulations is proposed to be amended as follows:

1. The authority citation shall continue to read as follows:

Authority: 12 U.S.C. 2601 et. seq.; 42 U.S.C. 3535(d).

2. In § 3500.2, paragraph (b) is amended by deleting the definition of Application, revising the definitions of Good faith estimate, and Mortgage broker and adding the following definitions of Final application, Final mortgage insurance costs disclosure, Guaranteed mortgage package, Loan originator, Loan settlement charges, Mortgage broker loan, Packager, Packaged services, Participating settlement service provider, Par value, Shopping application, and Unforeseeable and extraordinary circumstances:

Sec. 3500.2 Definitions.

(b) * * *

Final application means the submission, upon acceptance of a guaranteed mortgage package agreement or a good faith estimate, of credit information in anticipation of a credit decision, whether oral, written or electronic, relating to a federally related mortgage loan.

Final mortgage insurance costs disclosure means the disclosure described in § 3500.14(g)(1)(ix)(C).

Good faith estimate means an estimate of settlement costs on the required format prescribed at Appendix C to this part prepared in accordance with § 3500.7.

[[49159]]

Guaranteed loan settlement charge means an aggregate amount directly charged to the borrower for packaged services. Guaranteed loan settlement charge does not include (i) any charge of a type payable in a comparable cash transaction, (ii) lock-in fees, (iii) any amount charged to satisfy underwriting conditions, including conditions regarding the mortgage property's compliance with applicable laws and ordinances, (iv) any amount charged by a borrower-selected settlement service provider if different from the packager-selected provider of that service, and (v) charges due to unforeseeable and extraordinary circumstances.

Guaranteed mortgage package means a guaranteed loan settlement charge, estimated other required costs, and a conditional interest price (including both interest rate and discount points) for a federally related mortgage loan that is offered to a consumer under a Guaranteed Mortgage Package Agreement (GMPA) in accordance with § 3500.16.
* * * * *

Loan originator means a lender or mortgage broker.

* * * * *

Mortgage broker means a person or entity that renders origination services in a table funding or intermediary transaction. Where a mortgage broker is the source of the funds for a transaction, the mortgage broker is a "lender" for purposes of this part.

Mortgage broker loan is a federally related mortgage loan that is originated by a mortgage broker.

* * * * *

Packager means a person or other entity that offers guaranteed mortgage packages to borrowers in accordance with § 3500.16. Packager does not include a person or entity whose organizing charter does not permit engaging in primary mortgage market activities.

Packaged services are settlement services that the lender requires for settlement and includes all services except per diem interest, hazard insurance, escrow/reserves, mortgage insurance, flood insurance, and optional settlement services.

Participating settlement service provider means a settlement service provider that provides packaged services and whose charges are not imposed separately from the guaranteed loan settlement charge.

Par value means the principal amount of the loan.

* * * * *

Shopping application means the submission, together with any applicable fee, of credit information (Social Security number (including authorization to order a credit report with such number), property address, basic income information, the borrower's information on the house price or a best estimate on the value of the property, the mortgage loan amount and product type, and other reasonably requested information) by a borrower in anticipation of a guaranteed mortgage package offer or a good faith estimate, whether oral, written or electronic, relating to a federally related mortgage loan. If the submission does not state or identify a specific property, the submission is not a shopping application for a federally related mortgage loan under this part. The subsequent addition of an identified property to the submission converts the submission to a shopping application for a federally related mortgage loan.

* * * * *

Unforeseeable and extraordinary circumstances means acts of God, war, disaster, or any other emergency, making it impossible or impractical to perform.

* * * * *

3. In § 3500.7, the first sentence of paragraph (a) introductory text, paragraph (a)(1) and the first sentence of paragraph (b) are revised, and a new paragraph (g) is added to read as follows:

Sec. 3500.7 Good faith estimate

(a) Lender to provide. Except as provided in paragraphs (a) or (b) of this section, or where a guaranteed mortgage package agreement is provided in accordance with § 3500.16 of this part, the lender shall provide all borrowers who submit a shopping application with a good faith estimate of the amount of or range of charges for the specific settlement services the borrower is likely to incur in connection with the settlement. The lender shall provide the good faith estimate required under this section (a suggested format is set forth in appendix C of this part) either by delivering the good faith estimate or by placing it in the mail to the loan applicant, not later than three business days after the shopping application is received or prepared. A lender shall not collect any fee for providing the good faith estimate beyond that which is necessary to provide the good faith estimate.

(1) If the shopping application is denied or withdrawn before the end of the three business day period, the lender need not provide the borrower with a good faith estimate.

* * * * *

(b) Mortgage broker to provide. Except where a guaranteed mortgage package agreement is provided in accordance with § 3500.16 of this part, in the event a shopping application is received by a mortgage broker who is not an exclusive agent of the lender, the mortgage broker must provide a good faith estimate by delivering the good faith estimate or by placing it in the mail to the loan applicant, not later than three business days after a shopping application is received or prepared. As long as the mortgage broker has provided the good faith estimate, the funding lender is not required to provide an additional good faith estimate, but the funding lender is responsible for ascertaining that the good faith estimate has been delivered. If the shopping application is denied or withdrawn before the end of the three-business-day period, the mortgage broker need not provide the denied borrower with a good faith estimate. A mortgage broker shall not collect any fee for providing the good faith estimate beyond that which is necessary to provide the good faith estimate.

* * * * *

(g) Mortgage Broker Fee Agreement.

(1) *General.* Except where a guaranteed mortgage package agreement is provided in accordance with § 3500.16 of this part, each mortgage broker who is to receive mortgage broker compensation shall provide the loan applicant(s) a mortgage broker fee agreement in the format set forth in appendix [ ] of this part.

(2) *Content of mortgage broker fee agreement.* The mortgage broker fee agreement shall include--

(i) An explanation of the nature of the relationship between the applicant(s) and the mortgage broker and between the mortgage broker and the lender;

(ii) An explanation of how and to what extent, if any, the applicant's decisions in structuring the loan transaction may affect how the mortgage broker compensation is paid; and

(iii) The maximum amount of mortgage broker compensation, expressed as a dollar amount and/or a percentage of the loan amount, that the mortgage broker will receive.

(3) *Timing rules.* Subject to subsection (5) below, the mortgage broker fee agreement shall be provided in accordance with the timing rules for providing a good faith estimate set forth in section 3500.7. For open-end lines of credit, the mortgage broker fee agreement shall be delivered or placed in the mail not later than three business days after the shopping application is prepared or received.

(4) *Execution by mortgage broker and applicants.* The mortgage broker fee agreement shall be executed by the mortgage broker prior to providing it to the applicant(s). The applicant(s) may execute the mortgage broker fee agreement at any time, including at settlement.

(5) *Change in identity of mortgage broker.* If, after a shopping application is initially submitted by the applicant(s), another mortgage broker becomes involved in the mortgage loan transaction, the additional mortgage broker need not provide an additional mortgage broker fee agreement, so long as the total compensation payable to all mortgage brokers is within the maximum limit set forth in the initial mortgage broker fee agreement. If the total compensation payable to all mortgage brokers may exceed the maximum limit set forth in the initial mortgage broker fee agreement, a subsequent mortgage broker fee agreement must be provided within three business days of the initial involvement of the subsequent mortgage broker(s).

(6) *Sole obligation of mortgage broker.* The contractual obligation to comply with the mortgage broker fee agreement rests solely with the mortgage broker, and no other entity shall be liable for any misrepresentation or non-performance of the mortgage broker's obligations under the mortgage broker fee agreement, or the mortgage broker's collection of compensation in excess of the maximum compensation amount stated therein.

(7) *Preemption.* Pursuant to section 18 of RESPA, the Secretary determines that the mortgage broker fee agreement required by this section provides greater protection to consumers than disclosures required by state law. Therefore, all such laws are preempted to the extent they require different or additional disclosures.

* * * * *

[[49159]]

4. In § 3500.8, the third sentence of paragraph (a) is revised to read as follows:

Sec. 3500.8 Use of HUD-1 or HUD-1A settlement statements.

(a) * * * The GMP HUD-1 or GMP HUD-1A may be used for settlements involving a guaranteed mortgage package.

(b) * * *The settlement agent shall complete the HUD-1 or HUD-1A or the GMP HUD-1 or GMP HUD-1A in accordance with the instructions set forth in appendix A to this part.
* * * * *

5. In § 3500.10, the first sentence of paragraph (a) and paragraph (b) is revised and a new sentence is added to paragraph (e) to immediately follow the second sentence to read as follows:

Sec. 3500.10 One-day advance inspection of HUD-1 or HUD-1A settlement statement; delivery; record keeping.

(a) *Inspection one day prior to settlement upon request by the borrower.* The settlement agent shall permit the borrower, and, in loans subject to a guaranteed mortgage package agreement, the packager and the lender, to inspect the HUD-1 or HUD-1A or GMP HUD-1 or GMP HUD-1A settlement statement, completed to set forth those items that are known to the settlement agent at the time of inspection, during the business day immediately preceding settlement. * * *

(b) *Delivery.* The settlement agent shall provide a completed HUD-1 or HUD-1A or GMP HUD-1 or GMP HUD-1A to the borrower, the seller (if there is one), the packager, the lender (if the lender is not the settlement agent), and/or their agents. When the borrower's and seller's copies of the HUD-1 or HUD-1A or GMP HUD-1 or GMP HUD-1A differ as permitted by the instructions in Appendix A to this part, both copies shall be provided to the packager and the lender (if the lender is not the settlement agent). * * *
* * * * *

(e) * * * Packagers shall retain documentation of unforeseeable and extraordinary circumstances related to guaranteed mortgage package agreements provided to borrowers for five years after settlement.* * *
* * * * *

6. In § 3500.14, new paragraphs (g)(1)(viii), (g)(1)(ix) and (g)(1)(x) are added to read as follows:

Sec. 3500.14 Prohibition against kickbacks and unearned fees.

* * * * *
(g)(1)(viii) Subject to paragraph (4) of this subsection, a payment made or received by any person in connection with the provision of mortgage insurance services, if: (A) the borrower receives a guaranteed mortgage package agreement; (B) an estimate of the amount of mortgage insurance fees or premiums to be collected at settlement is separately disclosed on the guaranteed mortgage package agreement, together with the assumptions (e.g., the loan's loan-to-value ratio) on which the estimate is based (if the mortgage insurance is lender-paid, the estimate would be zero); (C) no later than 30 days following the borrowers' acceptance of a guaranteed mortgage package agreement and prior to settlement, a final mortgage insurance costs disclosure is provided to the borrower which includes the final amount of the mortgage insurance fees or premiums payable at or before settlement, together with an explanation, if the final amount exceeds the estimate, of the reason(s) why the final amount exceeds the estimate, and a statement that the mortgage insurance premiums or fees to be collected at or before settlement will not exceed the final amount of such premiums or fees set forth in the final mortgage insurance costs disclosure, unless the applicant requests a change in the amount or terms of the loan after the delivery of the final mortgage insurance costs; and (D) the packager complies with the cure procedures set forth in subsection [ ].

(g)(1)(ix) A payment made or received by any person in connection with an advertisement of settlement services. Any link, banner, brochure or other promotional message, whether communicated on an electronic medium or otherwise, whose characterization as an advertisement is unclear shall be deemed an advertisement for purposes of this section if it is accompanied by a clear and conspicuous notice indicating that it is an advertisement.

(g)(1)(x) Subject to clauses (A) and (B) below, all mortgage broker compensation that, in the aggregate, does not exceed the maximum mortgage broker compensation amount timely disclosed in the mortgage broker fee agreement required under section 3500.7(g).

(A) For purposes of the exemption in this subsection (x), a lender may rely on the dates and amounts set forth on the face of the mortgage broker fee agreement and any amounts and the recipients of amounts set forth on the face of the HUD-1 or HUD-1A;

(B) The exemption in this subsection (x) shall apply to any lender or mortgage broker if the lender or mortgage broker discovers that the mortgage broker compensation received by the mortgage broker exceeded the maximum mortgage broker compensation amount set forth in the mortgage broker fee agreement and the lender or mortgage broker refunds the excess compensation amount to the borrower within 60 days after the settlement date as reflected on the HUD-1 or HUD-1A settlement statement.

* * * * *

Sec. 3500.16 [Redesignated as Sec. 3500.20]

7. § 3500.16 is redesignated as § 3500.20 and a new § 3500.16 is added to read as follows:

Sec. 3500.16 Guaranteed Mortgage Package--Safe Harbor.

(a) General. A guaranteed mortgage package is defined in § 3500.2.

(b) Safe harbor. A guaranteed mortgage package, and any payment, discount, pricing arrangement or any other exchanges of things of value by and among packagers, lenders, and participating settlement service providers in connection with the provision of guaranteed mortgage packages shall not violate section 8 of RESPA or § 3500.14 if the guaranteed loan settlement charge collected at settlement does not exceed the guaranteed loan settlement charge disclosed in the guaranteed mortgage package agreement described in subsection (c)(3) below.

(c) Criteria for guaranteed mortgage package. Packagers must deliver a guaranteed mortgage package offer within 3 business days of a shopping application or such time as may be reasonable in special cases, provided that no guaranteed mortgage package offer is required if the shopping application is denied or withdrawn, that includes:

(1) A guaranteed loan settlement charge for packaged services that is effective from the time the guaranteed mortgage package is offered by the packager to the borrower through settlement provided that the borrower accepts the guaranteed mortgage package agreement within 10 days, or such greater period offered by the packager, from when the document is delivered or mailed to the borrower and settles the loan within a reasonable period specified by the packager or lender (which period shall be no shorter than the rate lock period selected by the applicant, if applicable);

(2) A mortgage loan with a conditional interest price (including both interest rate and discount points) that is applicable through settlement provided that (A) the borrower accepts the guaranteed mortgage package agreement within 10 days, or such greater period offered by the packager, and any interest price adjustments shall be ascertainable on the packager's website, via a local or toll-free telephone number, or other accessible media on a regular basis, and (B) the settlement occurs within a reasonable period specified by the packager or lender (which period shall be no shorter than the rate lock period selected by the applicant, if any); and

(3) A guaranteed mortgage package agreement as prescribed in and completed in conformity with Appendix F to this part which:

(i) Explains that the guaranteed mortgage package covers necessary settlement services required by the lender and discloses a guaranteed loan settlement charge for packaged services and estimated other required costs for non-packaged services that will apply to the loan;

[[49160]]

(ii) Identifies and provides estimates for other required settlement costs, such as per diem interest, reserves/escrow, hazard insurance, mortgage insurance, flood insurance, and optional owner's title insurance, and the amount of the lock-in fee, if any, and explains that any required settlement costs not separately itemized and estimated are the responsibility of the packager;

(iii) Identifies any applicable interest rate lock expiration period and the circumstances under which the lock-in fee, if any, will be refunded, which shall include any failure to close the mortgage loan offered in the guaranteed mortgage package within the rate lock period for reasons unrelated to and not caused, directly or indirectly, by the borrower;

(iv) Explains the borrower's ability to receive, upon request, information as to whether the lender has obtained a lender's valuation of the property, a lender's inspection of title, credit verification, and a pest inspection, and to receive, upon request, a copy of the pest inspection;

(v) Specifies that the packager will ensure that a mortgage loan is provided as part of the package and that, after acceptance by the borrower, the lender participating in the package shall, upon final loan approval, provide a loan in accordance with the guaranteed mortgage package agreement;

(vi) Advises the borrower of whether the loan has adjustable rate terms, whether there is a prepayment penalty, and whether there is a scheduled balloon payment, and that the borrower will receive Truth in Lending Act disclosures regarding his or her loan terms that he or she should review carefully;

(vii) Commits the packager and the borrower to the terms of the guaranteed mortgage package agreement upon borrower acceptance and payment of the fee permitted by § 3500.16 (c)(3)(ix)(A), subject only to acceptable final underwriting and property appraisal; and

(viii) Specifies that the packager will not charge (A) any fee to provide the offer of a guaranteed mortgage package beyond that fee which is estimated to offset the costs of providing such offer to the borrower, and (B) any other fee for the property valuation, credit report or other pre-closing services deemed necessary until acceptance by the borrower of the guaranteed mortgage package, *provided* the packager credits the amount of any such fee charged to the borrower under this section to the guaranteed loan settlement charge if such guaranteed mortgage package results in the borrower closing on the offered loan. In the case of a guaranteed mortgaged package made over the telephone, the packager may collect the fee permitted by this § 3500.16(c)(3)(viii)(A) so long as (I) the packager provides an abbreviated verbal disclosure of the contents of the guaranteed mortgage package, and the fact that a written guaranteed mortgage package agreement will be delivered to the borrower within three business days, and (II) the borrower orally accepts the guaranteed mortgage package over the telephone. Nothing in this section is intended to prevent a packager from charging a fee for locking in an interest rate at any time.

(d) Impact on Good faith estimate and HUD-1/1A. Where a packager satisfies the criteria in paragraph (c) of this section, the packager shall provide the borrower the guaranteed mortgage package agreement in lieu of the good faith estimate. In loans originated through guaranteed mortgage package agreements, the guaranteed loan settlement charge shall be shown as the origination fee on line 801 of the HUD-1/HUD-1A.

(e) Exclusions from safe harbor.

(1) Notwithstanding the existence of a guaranteed mortgage package, section 8 of RESPA remains applicable to payments by and between packagers or participating settlement service providers and parties outside the guaranteed mortgage package.

(2) The Affiliated Business Arrangement (AfBA) exemption requirements, set forth in § 3500.15, remain in effect when a borrower is referred to a packager by a person or entity not otherwise participating in the guaranteed mortgage package who is an affiliate of the packager or any participating settlement service provider.
(3) The exemption in this section shall not apply to a settlement agent that collects amounts for packaged services that exceed the Guaranteed Loan Settlement Charge in the guaranteed mortgage package agreement.

(f) Guaranteed Loan Settlement Charge Over-Collection. This subsection describes the procedures that must be followed if the packager provides the borrower with a guaranteed mortgage package agreement and the borrower believes in good faith that the amount of the guaranteed loan settlement charge disclosed on the HUD-1 or HUD 1-A erroneously exceeds the amount of such charge in the guaranteed mortgage package agreement.

(1) Definitions

(A) Guaranteed loan settlement charge over-collection. For purposes of this subsection, a guaranteed loan settlement charge over-collection is any excess of the guaranteed loan settlement charge collected or to be collected at settlement over the guaranteed loan settlement charge disclosed in the guaranteed mortgage package agreement, except that a guaranteed loan settlement charge over-collection does not include any increase in costs that is attributable to a request by the borrower for a change in the amount or terms of a loan after the packager has provided a guaranteed mortgage package agreement or to the borrower selecting a settlement service provider other than that generally used by the packager for packaged services.

(B) Guaranteed loan settlement charge over-collection notice. A guaranteed loan settlement charge over-collection notice is a written correspondence (other than notice on a payment coupon or other payment medium) that—

(i) is received—

(I) by the settlement agent at or before settlement; or

(II) by the packager that made the guaranteed mortgage package agreement, not later than one year after settlement (the packager may designate to the borrower a specific address to which this notice should be sent);

(ii) enables the person receiving the notice to identify the borrower's name, account number and address to which a refund may be sent; and

(iii) includes a statement of the amount of the alleged guaranteed loan settlement charge over-collection.

(2) Action with respect to the guaranteed loan settlement charge over-collection notice.

(A) If the guaranteed loan settlement charge over-collection notice is received by the settlement agent at or before settlement, then the settlement agent must—

(i) correct the alleged over-collection at or before settlement, and revise the HUD-1 or HUD 1-A accordingly, pursuant to instructions from the packager that made the guaranteed mortgage package agreement; or

(ii) forward the guaranteed loan settlement charge over-collection notice to such packager.

(B) If the guaranteed loan settlement charge over-collection notice is received by the packager who made the guaranteed mortgage package agreement (either directly from the borrower or from the settlement agent), then the packager must, within 30 business days of receiving the notice—

(i) refund the amount of the guaranteed loan settlement charge over-collection to the borrower; or

(ii) if the packager concludes that no over-collection occurred or that any over-collection was in an amount less than that alleged by the borrower, notify the borrower of its conclusion and the reasons for that conclusion, and refund any over-collection that was in an amount less than that alleged by the borrower.

(3) Additional payment. In addition to the amounts refunded pursuant to paragraph (f)(2) of this subsection, the packager must pay the borrower an amount equal to the guaranteed loan settlement charge over-collection refunded pursuant to paragraph (f)(2) unless—

(A) the over-collection is corrected at or before settlement pursuant to clause (f)(2)(A)(i);

(B) the packager corrects the over-collection within (i) 90 days from the date of closing or (ii) 90 days of discovering the over-collection, whichever is later, and before receiving a guaranteed loan settlement charge over-collection notice; or

(C) the packager concludes, after conducting an investigation that no over-collection occurred.

(4) Willful and Fraudulent Misconduct. Notwithstanding the guaranteed loan settlement charge over-collection resolution procedures of this subsection (f), the exemption provided by paragraph (b) of this section shall not apply to any packager or settlement service provider that engages in a pattern or practice of willfully and fraudulently imposing charges in excess of those permitted pursuant to paragraphs (c)(1)-(3).

(g) Loss of Safe Harbor. The loss of the safe harbor exemption because of an un-cured over-collection of guaranteed loan settlement charges affects the packager, the settlement agent and, if the packager is not the lender, the lender, but does not affect participating settlement service providers uninvolved in the settlement.

(h) Preemption of state law. Pursuant to section 18 of RESPA, the Secretary determines that the guaranteed mortgage package offered pursuant to this section is more beneficial for and gives greater protection to the consumer than any related state law. Therefore, the provisions of this section preempt any state law that conflicts with or frustrates the purpose of the offering of guaranteed mortgage packages under this section, including, but not limited to, state laws (1) imposing disclosures, (2) limiting fees (including loan related and referral fees) and rebates, (3) limiting the use of affiliated or unaffiliated providers, and (4) imposing advertising restrictions. The Secretary hereby finds that all such laws are inconsistent with the provisions of this section.

Sec. 3500.19 [Amended]

8. In § 3500.19(c) the cross-references to ``§ 3500.16" and to ``section 3500.16" are both revised to read ``§ 3500.20".

Blackline of CMC Recommended Changes
To HUD's Proposed Regulation

[[49158]]

VI. Rule Language

List of Subjects in 24 CFR part 3500

Consumer protection, Condominiums, Housing, Mortgagees, Mortgage servicing, Reporting, and recordkeeping requirements.

Accordingly, for the reasons set out in the preamble, part 3500 of title 24 of the Code of Federal Regulations is proposed to be amended as follows:

1. The authority citation shall continue to read as follows:

Authority: 12 U.S.C. 2601 et. seq.; 42 U.S.C. 3535(d).

2. In § 3500.2, paragraph (b) is amended by ~~revising~~ **deleting** the ~~definitions~~ **definition** of Application, **revising the definitions of** Good faith estimate, and Mortgage broker and adding the following definitions of **Final application, Final mortgage insurance costs disclosure,** Guaranteed mortgage package, Loan originator, **Loan settlement charges,** Mortgage broker loan, ~~No tolerance,~~ Packager, Packaged services, Participating settlement service provider, Par value, ~~Tolerance,~~ **Shopping application, and** Unforeseeable and extraordinary circumstances~~,~~ ~~and Zero tolerance~~:

Sec. 3500.2 Definitions.

* * * * *

(b) * * *

~~Application~~ **Final application** means the submission**, upon acceptance of a guaranteed mortgage package agreement or a good faith estimate,** of credit information ~~(Social Security number, property address, basic income information, the borrower's information on the house price or a best estimate on the value of the property, and the mortgage loan needed) by a borrower~~ in anticipation of a credit decision, whether oral, written or electronic, relating to a federally related mortgage loan.

~~If the submission does not state or identify a specific property, the submission is an application for a pre-qualification and not an application for a federally related mortgage loan under this part. The subsequent addition of an identified property to the submission converts the submission to an application for a federally related mortgage loan.~~

* * * * * **Final mortgage insurance costs disclosure means the disclosure described in § 3500.14(g)(1)(ix)(C).**

Good faith estimate means an estimate of settlement costs on the required format prescribed at Appendix C to this part prepared in accordance with ~~§3500.7. * * * * *~~ **§ 3500.7.**

~~[[49159]]~~ [[49159]]

Guaranteed loan settlement charge means an aggregate amount directly charged to the borrower for packaged services. Guaranteed loan settlement charge does not include (i) any charge of a type payable in a comparable cash transaction, (ii) lock-in fees, (iii) any amount charged to satisfy underwriting conditions, including conditions regarding the mortgage property's compliance with applicable laws and ordinances, (iv) any amount charged by a borrower-selected settlement service provider if different from the packager-selected provider of that service, and (v) charges due to unforeseeable and extraordinary circumstances.

Guaranteed mortgage package means a guaranteed ~~package of mortgage related settlement services and an interest rate guarantee~~ **loan settlement charge, estimated other required costs, and a conditional interest price (including both interest rate and discount points)** for a federally related mortgage loan that is offered to a consumer under a Guaranteed Mortgage Package Agreement (GMPA) in accordance with § 3500.16.
* * * * *

Loan originator means a lender or mortgage broker.
* * * * *

Mortgage broker means a person or entity that renders origination services in a table funding or intermediary transaction. Where a mortgage broker is the source of the funds for a transaction, the mortgage broker is a ~~``lender''~~**"lender"** for purposes of this part.
* * * * *

Mortgage broker loan is a federally related mortgage loan that is originated by a mortgage broker.
~~No tolerance means that the charges may vary without being subject to any tolerance.~~* * * * *

Packager means a person or other entity that offers ~~and provides~~ guaranteed mortgage packages to borrowers in accordance with § 3500.16. **Packager does not include a person or entity whose organizing charter does not permit engaging in primary mortgage market activities.**

Packaged services are settlement services that the lender requires for settlement and includes all services except per diem interest, hazard insurance, escrow/reserves, **mortgage insurance, flood insurance,** and optional settlement services.

Participating settlement service provider means a settlement service provider that provides ~~settlement~~ **packaged** services ~~in a guaranteed mortgage package~~ and whose charges are ~~included in~~ **not imposed separately from** the guaranteed ~~mortgage package price~~ **loan settlement charge**.

Par value means the principal amount of the loan.
* * * * *

Shopping application means the submission, together with any applicable fee, of credit information (Social Security number (including authorization to order a credit report with such number), property address, basic income information, the borrower's information on the house price or a best estimate on the value of the property, the mortgage loan amount and product type, and other reasonably requested information) by a borrower in anticipation of a guaranteed mortgage package offer or a good faith estimate, whether oral, written or electronic, relating to a federally related mortgage loan. If the submission does not state or identify a specific property, the submission is not a shopping application for a federally related mortgage loan under this part. The subsequent addition of an identified property to the submission converts the submission to a shopping application for a federally related mortgage loan.
* * * * *~~Tolerance means a variation above an estimate of a category of settlement costs. Tolerance is expressed as a percentage of the estimate.~~

Unforeseeable and extraordinary circumstances means acts of God, war, disaster, or any other emergency, making it impossible or impractical to perform.
~~Zero tolerance means the amount listed may not vary at closing, except in unforeseeable and extraordinary circumstances.~~
* * * * *

3. In § 3500.7, **the first sentence of** paragraph (a) introductory text ~~and (a)(2) through (e) are revised, paragraph (f) is redesignated as paragraph (g); and a new paragraph (f)~~**, paragraph (a)(1) and the first sentence of paragraph (b) are revised, and a new paragraph (g)** is added to read as follows:

Sec. 3500.7 Good faith estimate

(a) Lender to provide. Except as provided in paragraphs (a)~~,~~ **or** (b) ~~or (f)~~ of this section, or where a guaranteed mortgage package agreement is provided in accordance with § 3500.16 of this part, the lender shall provide all ~~applicants for a federally related mortgage loan~~ **borrowers who submit a shopping application** with a good faith estimate **of the amount of or range of charges for the specific settlement services the borrower is likely to incur in connection with the settlement**. The lender shall provide the good faith estimate **required under this section (a suggested format is set forth in appendix C of this part)** either by delivering the good faith estimate or by placing it in the mail to the loan applicant, not later than three business days after ~~an~~ **the shopping** application is received or prepared. ~~If the application is denied before the end of the three-business-day period, the lender need not provide the denied borrower with a good faith estimate.~~ A lender shall not collect any fee ~~in connection with the application or~~ **for providing** the good faith estimate beyond that which is necessary to provide the good faith estimate.

~~* * * * *~~**(1) If the shopping application is denied or withdrawn before the end of the three business day period, the lender need not provide the borrower with a good faith estimate.**
~~(2) For all mortgage loans, third party settlement services, governmental fees and charges, any other loan related expenses that are not paid to and retained by the originator must be reported in their entirety in the appropriate categories on the good faith estimate.~~
~~* * * * *~~*** * * * ***

(b) Mortgage broker to provide. ~~In the event an~~ **Except where a guaranteed mortgage package agreement is provided in accordance with § 3500.16 of this part, in the event a shopping** application is received by a mortgage broker who is not an exclusive agent of the lender, the mortgage broker must provide a good faith estimate by delivering the good faith estimate or by placing it in the mail to the loan applicant, not later than three business days after ~~an~~ **a shopping** application is received or prepared. As long as the mortgage broker has provided the good faith estimate, the funding lender is not required to provide an additional good faith estimate, but the funding lender is responsible for ascertaining that the good faith estimate has been delivered. If the **shopping** application is denied **or withdrawn** before the end of the three-business-day period, the mortgage broker need not provide the denied borrower with a good faith estimate. A mortgage broker shall not collect any fee ~~in connection with the application or~~ **for providing** the good faith estimate beyond that which **is** necessary to provide the good faith estimate.
*** * * * ***

(g) Mortgage Broker Fee Agreement.

(1) *General.* Except where a guaranteed mortgage package agreement is provided in accordance with § 3500.16 of this part, each mortgage broker who is to receive mortgage broker compensation shall provide the loan applicant(s) a mortgage broker fee agreement in the format set forth in appendix [ ] of this part.

(2) *Content of mortgage broker fee agreement.* The mortgage broker fee agreement shall include—

(i) An explanation of the nature of the relationship between the applicant(s) and the mortgage broker and between the mortgage broker and the lender;

(ii) An explanation of how and to what extent, if any, the applicant's decisions in structuring the loan transaction may affect how the mortgage broker compensation is paid; and

(iii) The maximum amount of mortgage broker compensation, expressed as a dollar amount and/or a percentage of the loan amount, that the mortgage broker will receive.

(3) *Timing rules.* Subject to subsection (5) below, the mortgage broker fee agreement shall be provided in accordance with the timing rules for providing a~~(c) Content of good faith estimate. As prescribed in and completed in accordance with the instructions in Appendix C to this part, the good faith estimate must state the property address, loan amount, interest rate used to calculate the estimated amounts, the Annual Percentage Rate (APR) for the loan including mortgage insurance, and the monthly payment for principal and interest and mortgage insurance. The form must also state whether the loan is an adjustable rate mortgage, contains a prepayment penalty clause or has a~~

~~balloon payment, the functions of the originator, and the total amount of charges for each category of services: loan origination, interest rate dependent payment, lender required and selected third party services, title services and title insurance, shoppable lender required third party services, government services, amounts for escrow/reserves, per diem interest, hazard insurance and optional owner's title insurance. Attachment A-1 of the~~ good faith estimate ~~must indicate the subtotals of the origination charges to the lender and to~~ **set forth in section 3500.7. For open-end lines of credit, the mortgage broker fee agreement shall be delivered or placed in the mail not later than three business days after the shopping application is prepared or received.**

(4) Execution by mortgage broker and applicants. **The mortgage broker fee agreement shall be executed by the mortgage broker prior to providing it to the applicant(s). The applicant(s) may execute the mortgage broker fee agreement at any time, including at settlement.**

(5) Change in identity of mortgage broker. **If, after a shopping application is initially submitted by the applicant(s), another mortgage broker becomes involved in the mortgage loan transaction, the additional mortgage broker need not provide an additional mortgage broker fee agreement, so long as the total compensation payable to all mortgage brokers is within the maximum limit set forth in the initial mortgage broker fee agreement. If the total compensation payable to all mortgage brokers may exceed the maximum limit set forth in the initial mortgage broker fee agreement, a subsequent mortgage broker fee agreement must be provided within three business days of the initial involvement of the subsequent mortgage broker(s).**

(6) Sole obligation of mortgage broker. **The contractual obligation to comply with the mortgage broker fee agreement rests solely with** the mortgage broker, and ~~the subtotals of all the charges and fees for title and for settlement agent services.~~

~~(d) Accuracy of good faith estimate. (1) The amounts of the categories of loan origination charges, lender required and selected third party settlement service provider charges, lender selected title services and title insurance, and governmental fees and charges reported on the good faith estimate shall not vary from the time the good faith estimate is given to the borrower and may not be exceeded at settlement absent unforeseeable and extraordinary circumstances. The estimates in the good faith estimate shall be open to the borrower for a minimum of 30 days from when the document is delivered or mailed to the borrower. Within the 30 days the borrower must agree to go forward and pay the additional money to complete the underwriting process. If the offer expires, the borrower may ask the loan originator to ratify such estimate or request a new one. If the cost at settlement exceeds the estimate reported on the good faith estimate, absent unforeseeable and extraordinary circumstances, the borrower may withdraw the application and receive a full refund of all loan related fees and charges. The loan originator must document any such circumstances and retain the document in accordance with § 3500.10(e).~~

~~(2) The amounts for lender required third party services must include an estimate of the maximum mortgage insurance premium to be charged upfront to the borrower based upon the borrower's assertion of the value of the property and loan amount needed and indicate that the mortgage insurance premium may decrease or be removed after full underwriting;~~

~~(3) The amounts of the categories of borrower selected title services and title insurance, shoppable lender required third party services, and reserves/escrow deposits charged to a borrower may not vary at settlement by greater~~

~~[[49159]]~~

~~than a tolerance of 10% from the amounts for such categories reported on the good faith estimate, except when a borrower chooses to purchase a more expensive service, absent unforeseeable and extraordinary circumstances.~~

~~(4) The amounts of the categories of per diem interest, hazard insurance and optional owner's title insurance reported on the good faith estimate shall be carefully prepared based upon the originator's knowledge of relevant prices, but are not subject to tolerances, which means that charges may vary without being subject to any tolerance.~~

~~(5) In mortgage broker loans, the borrower payment to the lender for a lower interest rate must be paid in full to the lender and the lender payment to the borrower for a higher rate must include any lender payments for the transaction other than for the par value of the loan.~~
~~(6) Loan originators must include all charges correctly within their prescribed category on the good faith estimate and not include any ``mark ups'' or ``up charges'' in their estimates of charges for categories III(C) through (J) of the good faith estimate. The Loan originator shall include all of its charges in the origination charges and interest rate dependent categories.~~
~~(7) No loan originator shall be held responsible for charges imposed on the borrower at settlement for shoppable lender required third party services unless the borrower asked where the services could be obtained within the tolerance, used a settlement service provider identified by the originator, and was charged an amount in excess of the tolerance.~~
~~(e) Form of good faith estimate. A good faith estimate required format is set forth in Appendix C to this part. The good faith estimate may be provided together with disclosures required by the Truth in Lending Act, 15 U.S.C. 1601 et seq., so long as all required material for the good faith estimate is grouped together.~~
~~(f) Particular providers required by lender. (1) If the lender requires the use (see § 3500.2, ``required use'') of a particular provider of a settlement service, other than the lender's own employees, and also requires the borrower to pay any portion of the cost of such service, the good faith estimate must identify the required settlement service provider.~~
~~(2) Except for a provider that is the lender's chosen attorney, credit reporting agency, or appraiser, if the lender is in an affiliated business relationship (see § 3500.15) with a provider, the lender may not require the use of that provider.~~
~~(3) If the lender maintains a controlled list of required providers (five or more for each discrete service) or relies on a list maintained by others, and at the time of application the lender has not yet decided which provider will be selected from that list, then the lender may satisfy the requirements of this section if the lender provides the borrower, on the good faith estimate, with the names of the required providers, and the estimated charge for the particular settlement service.~~
~~* * * * *~~**no other entity shall be liable for any misrepresentation or non-performance of the mortgage broker's obligations under the mortgage broker fee agreement, or the mortgage broker's collection of compensation in excess of the maximum compensation amount stated therein.**

(7) *Preemption.* Pursuant to section 18 of RESPA, the Secretary determines that the mortgage broker fee agreement required by this section provides greater protection to consumers than disclosures required by state law. Therefore, all such laws are preempted to the extent they require different or additional disclosures.
* * * * *

[[49159]]

4. In § 3500.8, the third sentence of paragraph (a) is revised to read as follows:

Sec. 3500.8 Use of HUD-1 or HUD-1A settlement statements.

(a) * * * ~~Alternatively, the form~~ **The GMP HUD-1 or GMP** HUD-1A may be used for ~~these transactions, but not for transactions in which there is a lender credit to the borrower. * * *~~**settlements involving a guaranteed mortgage package.**

(b) * * *The settlement agent shall complete the HUD-1 or HUD-1A or the GMP HUD-1 or GMP HUD-1A in accordance with the instructions set forth in appendix A to this part.
* * * * *

5. In § 3500.10, **the first sentence of paragraph (a) and paragraph (b) is revised and** a new sentence is added to paragraph (e) to immediately follow the second sentence to read as follows:

Sec. 3500.10 One-day advance inspection of HUD-1 or HUD-1A settlement statement; delivery; ~~recordkeeping.~~ record keeping.

~~(e) * * * Loan originators shall retain documentation of unforeseeable and extraordinary circumstances related to good faith estimates provided to borrowers and packagers shall retain documentation of such circumstances related to~~ (a) *Inspection one day prior to settlement upon request by the borrower.* The settlement agent shall permit the borrower, and, in loans subject to a guaranteed mortgage package ~~agreements provided to borrowers for five years after settlement.* * *~~agreement, the packager and the lender, to inspect the HUD-1 or HUD-1A or GMP HUD-1 or GMP HUD-1A settlement statement, completed to set forth those items that are known to the settlement agent at the time of inspection, during the business day immediately preceding settlement. * * *

~~* * * * *~~(b) *Delivery.* The settlement agent shall provide a completed HUD-1 or HUD-1A or GMP HUD-1 or GMP HUD-1A to the borrower, the seller (if there is one), the packager, the lender (if the lender is not the settlement agent), and/or their agents. When the borrower's and seller's copies of the HUD-1 or HUD-1A or GMP HUD-1 or GMP HUD-1A differ as permitted by the instructions in Appendix A to this part, both copies shall be provided to the packager and the lender (if the lender is not the settlement agent). * * *
~~6. In § 3500.14, a new paragraph (g)(1)(viii) is~~* * * * *

(e) * * * Packagers shall retain documentation of unforeseeable and extraordinary circumstances related to guaranteed mortgage package agreements provided to borrowers for five years after settlement.* * *
* * * * *

6. In § 3500.14, new paragraphs (g)(1)(viii), (g)(1)(ix) and (g)(1)(x) are added to read as follows:

Sec. 3500.14 Prohibition against kickbacks and unearned fees.

* * * * *

(g)(1)(viii) ~~Any discounts negotiated among settlement service providers, packagers, or any other entities for settlement services provided that the entire discounted price is charged to the borrower and reported as part of the total charge within Sections III(C) through (J) of the good faith estimate as appropriate.~~ Subject to paragraph (4) of this subsection, a payment made or received by any person in connection with the provision of mortgage insurance services, if: (A) the borrower receives a guaranteed mortgage package agreement; (B) an estimate of the amount of mortgage insurance fees or premiums to be collected at settlement is separately disclosed on the guaranteed mortgage package agreement, together with the assumptions (e.g., the loan's loan-to-value ratio) on which the estimate is based (if the mortgage insurance is lender-paid, the estimate would be zero); (C) no later than 30 days following the borrowers' acceptance of a guaranteed mortgage package agreement and prior to settlement, a final mortgage insurance costs disclosure is provided to the borrower which includes the final amount of the mortgage insurance fees or premiums payable at or before settlement, together with an explanation, if the final amount exceeds the estimate, of the reason(s) why the final amount exceeds the estimate, and a statement that the mortgage insurance premiums or fees to be collected at or before settlement will not exceed the final amount of such premiums or fees set forth in the final mortgage insurance costs disclosure, unless the applicant requests a change in the amount or terms of the loan after the delivery of the final mortgage insurance costs; and (D) the packager complies with the cure procedures set forth in subsection [ ].

(g)(1)(ix) A payment made or received by any person in connection with an advertisement of settlement services. Any link, banner, brochure or other promotional message, whether communicated on an electronic medium or otherwise, whose characterization as an advertisement is unclear shall be deemed an advertisement for purposes of this section if it is accompanied by a clear and conspicuous notice indicating that it is an advertisement.

(g)(1)(x) Subject to clauses (A) and (B) below, all mortgage broker compensation that, in the aggregate, does not exceed the maximum mortgage broker compensation amount timely disclosed in the mortgage broker fee agreement required under section 3500.7(g).

(A) For purposes of the exemption in this subsection (x), a lender may rely on the dates and amounts set forth on the face of the mortgage broker fee agreement and any amounts and the

recipients of amounts set forth on the face of the HUD-1 or HUD-1A;

(B) The exemption in this subsection (x) shall apply to any lender or mortgage broker if the lender or mortgage broker discovers that the mortgage broker compensation received by the mortgage broker exceeded the maximum mortgage broker compensation amount set forth in the mortgage broker fee agreement and the lender or mortgage broker refunds the excess compensation amount to the borrower within 60 days after the settlement date as reflected on the HUD-1 or HUD-1A settlement statement.

* * * * *

Sec. 3500.16 [Redesignated as Sec. 3500.20]

7. ~~In~~§ 3500.16 is redesignated as § 3500.20 and a new § 3500.16 is added to read as follows:

Sec. 3500.16 Guaranteed Mortgage Package--Safe Harbor.

(a) General. A guaranteed mortgage package is defined in § 3500.2.

(b) ~~Violation and safe~~ **Safe** harbor. A guaranteed mortgage package, ~~including payments, discounts,~~ **and any payment, discount,** pricing ~~arrangements~~ **arrangement** or any other exchanges of things of value by and ~~between persons or entities offering their services and compensated through guaranteed mortgage packages (hereinafter ``packagers'')~~ **among packagers, lenders,** and participating settlement service providers ~~as part of such a transaction,~~ **in connection with the provision of guaranteed mortgage packages** shall not violate section 8 of RESPA or § 3500.14 ~~and satisfies sections 4 and 5 of RESPA if the conditions set forth in this section are met.~~ **if the guaranteed loan settlement charge collected at settlement does not exceed the guaranteed loan settlement charge disclosed in the guaranteed mortgage package agreement described in subsection (c)(3) below.**

(c) Criteria for guaranteed mortgage package. ~~In order to qualify for the safe harbor stated in paragraph (b) of this section, packagers~~ **Packagers** must deliver a guaranteed mortgage package offer within 3 **business** days of **a shopping** application or such time as may be reasonable in special cases ~~but prior to the borrower paying any fee,~~ **provided that no guaranteed mortgage package offer is required if the shopping application is denied or withdrawn**, that includes:

(1) A ~~package of designated lender required~~ **guaranteed loan** settlement **charge for packaged** services ~~at a guaranteed price~~ **that is effective** from the time the guaranteed mortgage package is offered by the packager to the borrower through settlement provided that the borrower accepts the guaranteed mortgage package agreement within ~~30~~ **10** days, or such greater period offered by the packager, from when the document is delivered or mailed to the borrower **and settles the loan within a reasonable period specified by the packager or lender (which period shall be no shorter than the rate lock period selected by the applicant, if applicable)**;

(2) A mortgage loan with ~~an interest rate guarantee and an Annual Percentage Rate (APR) that is guaranteed~~ **a conditional interest price (including both interest rate and discount points) that is applicable** through settlement provided that **(A)** the borrower accepts the guaranteed mortgage package agreement within ~~30~~ **10** days, or such greater period offered by the packager, and ~~the interest rate is adjusted only to reflect changes in market interest rates based on movement in a observable and verifiable index or other appropriate measure~~ **any interest price adjustments shall be ascertainable on the packager's website, via a local or toll-free telephone number, or other accessible media on a regular basis, and (B) the settlement occurs within a reasonable period specified by the packager or lender (which period shall be no shorter than the rate lock period selected by the applicant, if any)**; and

(3) A guaranteed mortgage package agreement as prescribed in and completed in conformity with Appendix F to this part which:

(i) Explains that the guaranteed mortgage package ~~includes~~ **covers** necessary settlement services required by the lender and ~~guarantees a package price for these services through settlement provided that the borrower accepts the~~

~~GMPA within 30 days, or such greater period offered by the packager, from when the document is delivered or mailed to the borrower;~~ **discloses a guaranteed loan settlement charge for packaged services and estimated other required costs for non-packaged services that will apply to the loan;**

~~**(ii) Commits the packager to provide all settlement services and includes all charges required to complete your mortgage except those specified as other required settlement costs and advises the borrower if the packager anticipates whether a pest inspection, lender's title**~~ **[[49160]]**

~~[[49160]]~~

~~insurance, credit report, and/or appraisal will be anticipated;~~
~~(iii)~~**(ii)** Identifies and provides estimates for other required settlement costs, such as per diem interest, reserves/escrow, ~~and hazard~~ **hazard insurance, mortgage insurance, flood** insurance, and optional owner's title insurance**, and the amount of the lock-in fee, if any,** and explains that any required settlement costs not separately itemized and estimated are the responsibility of the packager;

~~(iv) Identifies and explains any borrower option to utilize payments to or from the lender as a result of the interest rate to pay settlement costs or adjust the interest rate and mortgage payments;~~
~~(v) Identifies any reports such as the pest inspection, lender's title insurance, appraisal or credit report for the loan transaction that are available to the borrower at the borrower's request;~~
~~(vi) Specifies that the packager will ensure that a mortgage loan is provided as part of the package and that, after acceptance by the borrower and the lender, the lender participating in the package shall provide a loan with the same terms as set forth~~**(iii) Identifies any applicable interest rate lock expiration period and the circumstances under which the lock-in fee, if any, will be refunded, which shall include any failure to close the mortgage loan offered** in the guaranteed mortgage package ~~agreement;~~ **within the rate lock period for reasons unrelated to and not caused, directly or indirectly, by the borrower;**

~~(vii) Advises the borrower of whether the loan is an adjustable rate mortgage and the terms of the mortgage, whether there is a prepayment penalty and that the borrower can request its terms, whether there is a balloon payment, whether the guaranteed mortgage package price includes an upfront maximum mortgage insurance premium based upon the borrowers assertion of the value of the property and loan amount needed and that the mortgage insurance premium may decrease or be removed after full underwriting; and~~**(iv) Explains the borrower's ability to receive, upon request, information as to whether the lender has obtained a lender's valuation of the property, a lender's inspection of title, credit verification, and a pest inspection, and to receive, upon request, a copy of the pest inspection;**

~~(viii) Commits the packager to the terms of~~**(v) Specifies that the packager will ensure that a mortgage loan is provided as part of the package and that, after acceptance by the borrower, the lender participating in the package shall, upon final loan approval, provide a loan in accordance with** the guaranteed mortgage package agreement**;**

(vi) Advises the borrower of whether the loan has adjustable rate terms, whether there is a prepayment penalty, and whether there is a scheduled balloon payment, and that the borrower will receive Truth in Lending Act disclosures regarding his or her loan terms which he or she should review carefully;

(vii) Commits the packager and the borrower to the terms of the guaranteed mortgage package agreement upon borrower acceptance and payment of ~~any fee~~ **the fee permitted by § 3500.16 (c)(3)(ix)(A)**, subject only to acceptable final underwriting and property appraisal**; and**

(viii) Specifies that the packager will not charge (A) any fee to provide the offer of a guaranteed mortgage package beyond that fee which is estimated to offset the costs of providing such offer to the borrower, and (B) any other fee for the property valuation, credit report or other pre-closing services deemed necessary until acceptance by the borrower of the guaranteed mortgage package, *provided* the packager credits the amount of any such fee charged to the borrower under this section to the guaranteed loan settlement charge if such guaranteed mortgage package results in the borrower closing on the offered loan. In the case of a guaranteed

mortgaged package made over the telephone, the packager may collect the fee permitted by this § 3500.16(c)(3)(viii)(A) so long as (I) the packager provides an abbreviated verbal disclosure of the contents of the guaranteed mortgage package, and the fact that a written guaranteed mortgage package agreement will be delivered to the borrower within three business days, and (II) the borrower orally accepts the guaranteed mortgage package over the telephone. Nothing in this section is intended to prevent a packager from charging a fee for locking in an interest rate at any time.

(d) Impact on Good faith estimate and HUD-1/1A. Where a packager satisfies the criteria in paragraph (c) of this section, the packager shall provide the borrower the guaranteed mortgage package agreement in lieu of the good faith estimate. In loans originated through guaranteed mortgage package agreements, the ~~HUD-1/1-A shall be completed at settlement by itemizing all the included services (but not the charges) of third party settlement service providers that were performed for the guaranteed mortgage package price. The guaranteed mortgage package price~~ **guaranteed loan settlement charge** shall be shown as the origination fee on line 801 of the HUD-~~1/ HUD-1A. Additionally, the packager must list the finance charges needed to calculate the APR on an addendum to the HUD-1 or HUD~~ **1/HUD**-1A.

(e) Exclusions from safe harbor.

(1) Notwithstanding the existence of a guaranteed mortgage package, section 8 of RESPA remains applicable to payments by and between packagers or participating settlement service providers and parties outside the guaranteed mortgage package.

(2) The Affiliated Business Arrangement (AfBA) exemption requirements, set forth in § 3500.15, remain in effect when a borrower is referred to a packager by a person or entity not otherwise participating in the guaranteed mortgage package who is an affiliate of the packager or any participating settlement service provider.

(3) The **exemption in this section shall not apply to a settlement agent that collects amounts for packaged services that exceed the Guaranteed Loan Settlement Charge in the** guaranteed mortgage package ~~safe harbor shall not be available where the rate or points and fees of a Federally related mortgage loan make the loan subject to the Home Ownership Equity Protection Act (HOEPA).~~ **agreement.**

(f) Guaranteed Loan Settlement Charge Over-Collection. This subsection describes the procedures that must be followed if the packager provides the borrower with a guaranteed mortgage package agreement and the borrower believes in good faith that the amount of the guaranteed loan settlement charge disclosed on the HUD-1 or HUD 1-A erroneously exceeds the amount of such charge in the guaranteed mortgage package agreement.

(1) Definitions

(A) Guaranteed loan settlement charge over-collection. For purposes of this subsection, a guaranteed loan settlement charge over-collection is any excess of the guaranteed loan settlement charge collected or to be collected at settlement over the guaranteed loan settlement charge disclosed in the guaranteed mortgage package agreement, except that a guaranteed loan settlement charge over-collection does not include any increase in costs that is attributable to a request by the borrower for a change in the amount or terms of a loan after the packager has provided a guaranteed mortgage package agreement or to the borrower selecting a settlement service provider other than that generally used by the packager for packaged services.

(B) Guaranteed loan settlement charge over-collection notice. A guaranteed loan settlement charge over-collection notice is a written correspondence (other than notice on a payment coupon or other payment medium) that—

(i) is received—

(I) by the settlement agent at or before settlement; or

(II) by the packager that made the guaranteed mortgage package agreement, not later than one year after settlement (the packager may designate to the borrower a specific address to which this notice should be sent);

(ii) enables the person receiving the notice to identify the borrower's name, account number and address to which a refund may be sent; and

(iii) includes a statement of the amount of the alleged guaranteed loan settlement charge over-collection.

(2) Action with respect to the guaranteed loan settlement charge over-collection notice.

(A) If the guaranteed loan settlement charge over-collection notice is received by the settlement agent at or before settlement, then the settlement agent must—

(i) correct the alleged over-collection at or before settlement, and revise the HUD-1 or HUD 1-A accordingly, pursuant to instructions from the packager that made the guaranteed mortgage package agreement; or

(ii) forward the guaranteed loan settlement charge over-collection notice to such packager.

(B) If the guaranteed loan settlement charge over-collection notice is received by the packager who made the guaranteed mortgage package agreement (either directly from the borrower or from the settlement agent), then the packager must, within 30 business days of receiving the notice—

(i) refund the amount of the guaranteed loan settlement charge over-collection to the borrower; or

(ii) if the packager concludes that no over-collection occurred or that any over-collection was in an amount less than that alleged by the borrower, notify the borrower of its conclusion and the reasons for that conclusion, and refund any over-collection that was in an amount less than that alleged by the borrower.

(3) Additional payment. In addition to the amounts refunded pursuant to paragraph (f)(2) of this subsection, the packager must pay the borrower an amount equal to the guaranteed loan settlement charge over-collection refunded pursuant to paragraph (f)(2) unless—

(A) the over-collection is corrected at or before settlement pursuant to clause (f)(2)(A)(i);

(B) the packager corrects the over-collection within (i) 90 days from the date of closing or (ii) 90 days of discovering the over-collection, whichever is later, and before receiving a guaranteed loan settlement charge over-collection notice; or

(C) the packager concludes, after conducting an investigation, that no over-collection occurred.

(4) Willful and Fraudulent Misconduct. Notwithstanding the guaranteed loan settlement charge over-collection resolution procedures of this subsection (f), the exemption provided by paragraph (b) of this section shall not apply to any packager or settlement service provider that engages in a pattern or practice of willfully and fraudulently imposing charges in excess of those permitted pursuant to paragraphs (c)(1)-(3).

(g) Loss of Safe Harbor. The loss of the safe harbor exemption because of an un-cured over-collection of guaranteed loan settlement charges affects the packager, the settlement agent and, if the packager is not the lender, the lender, but does not affect participating settlement service providers

uninvolved in the settlement.

(h) Preemption of state law. Pursuant to section 18 of RESPA, the Secretary determines that the guaranteed mortgage package offered pursuant to this section is more beneficial for and gives greater protection to the consumer than any related state law. Therefore, the provisions of this section preempt any state law that conflicts with or frustrates the purpose of the offering of guaranteed mortgage packages under this section, including, but not limited to, state laws (1) imposing disclosures, (2) limiting fees (including loan related and referral fees) and rebates, (3) limiting the use of affiliated or unaffiliated providers, and (4) imposing advertising restrictions. The Secretary hereby finds that all such laws are inconsistent with the provisions of this section.

Sec. 3500.19 [Amended]

8. In § 3500.19(c) the cross references to ``§ 3500.16" and to ``section 3500.16" are both revised to read ``§ 3500.20".

Tab 4

Guaranteed Mortgage Package Agreement

This GUARANTEED MORTGAGE PACKAGE AGREEMENT ("Agreement") commits us, ______________ the PACKAGER, to provide you, ________________________________ the BORROWER(S), upon your acceptance within ____________ days [*10 days or greater*] of the date this form is delivered or mailed to you:

(1) a mortgage loan on the property described below at a CONDITIONAL INTEREST PRICE;
(2) a GUARANTEED LOAN SETTLEMENT CHARGE for packaged settlement services required by the lender;
(3) an estimate of the amount of OTHER REQUIRED SETTLEMENT COSTS you will pay at or before settlement; and
(4) a sum of the TOTAL ESTIMATED SETTLEMENT COSTS that you will be required to pay at or before settlement to obtain your mortgage.

Upon acceptance of this Agreement, you will be required to pay a $ _____ application-related fee, which will be included in the Guaranteed Loan Settlement Charge. This fee is nonrefundable except [*insert terms of refundability, if any*]. *[Describe any other pre-closing fees (i.e. commitment fees) that may apply and their terms of refundability.]*

This Agreement is subject to verification of your credit rating, final property appraisal, and other appropriate underwriting criteria and is based on the loan amount and loan product specified below. If you change the loan amount or loan product specified below, you will receive a new Guaranteed Mortgage Package Agreement reflecting those new terms upon obtaining final approval for your loan. Other providers offer similar packages, or alternative approaches to mortgage origination. You should shop to find the best packager and mortgage product to meet your needs. For more information regarding guaranteed mortgage packages and their costs, see the Special Information Booklet provided to you with this Agreement.

<u>THE PROPERTY</u>: You seek to [purchase] [refinance] a residential property at
(Address) ____

I. <u>CONDITIONAL INTEREST PRICE</u>

We will provide you with a conditional interest price of ___% with [ ] points* on a [*fixed rate*] [*adjustable rate*] mortgage** of $________ for [ ] years.
<u>Loan Product:</u> The specific loan product on which this Agreement is based is: [*insert loan product type including rate lock period or required settlement date*]

This Conditional Interest Price is applicable through settlement if you accept and sign this Agreement now and [have locked in this rate or lock in this rate by [*insert date/time*]]. If you accept and sign this Agreement now but choose not to lock-in the interest rate until a later date, you may monitor your loan product, including the price (in terms of the interest rate and discount points) and the rate lock period that applies to your loan product. Contact us at [*insert website and/or local or toll free telephone number*]. If you do not accept and sign this Agreement now, you must accept and sign this Agreement within [ ] [*10 days or greater*] from [*insert date*] or the offer will expire.

<u>Rate Lock Period and Lock-In Fee</u>. Once locked in, this Conditional Interest Price will remain fixed for __ days ("rate lock period"). The lock-in fee for locking in the Conditional Interest Price for the rate lock period is $ ___. This fee is listed as an Other Required Settlement Cost in Section III below. This fee will will not be credited

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* This conditional interest price (including both the interest rate and discount points) is subject to final underwriting and appraisal. You may be able to adjust your selection of interest rate/discount points combination. You should ask your packager about combinations available to you.

** You will receive Truth-in-Lending Act disclosures regarding your loan terms and an Adjustable Rate Mortgage disclosure, if applicable, that you should review carefully.

to you at closing. This fee will be refunded if the mortgage loan offered in this Agreement fails to close within the rate lock period for reasons unrelated to, and not caused, either directly or indirectly, by you. Other lock options may be available. Ask us for details.

Settlement Date. Upon acceptance of this Agreement, settlement must occur within the rate lock period applicable to your loan product as specified above, if you have locked the rate, or if no rate lock period applies by [*insert date*]. If we permit an extension of these periods, extension fees may apply. Extension fees are not included in the Guaranteed Loan Settlement Charge.

II. GUARANTEED LOAN SETTLEMENT CHARGE

We provide you a GUARANTEED LOAN SETTLEMENT CHARGE for packaged settlement services required to complete your mortgage. This GUARANTEED LOAN SETTLEMENT CHARGE does not include (i) any charge of a type payable in a comparable cash transaction, (ii) any amount charged to satisfy underwriting conditions, including conditions regarding the mortgage property's compliance with applicable laws and ordinances, (iii) any amount charged by a borrower-selected settlement service provider if different from the packager-selected provider of that service, and (iv) charges due to unforeseeable and extraordinary circumstances. You will pay this GUARANTEED LOAN SETTLEMENT CHARGE in addition to the OTHER REQUIRED SETTLEMENT COSTS itemized in Section III. The precise services for each transaction may vary.

Upon request we will notify you whether we have obtained certain reports, such as a pest inspection, our valuation of the property, our inspection of title and/or a credit verification, if any. Upon request, we will provide you with a copy of any pest inspection report we receive.

The GUARANTEED LOAN SETTLEMENT CHARGE may vary if: (i) the loan amount or loan product changes; and/or (ii) you select settlement service providers for packaged services other than those we generally use.

GUARANTEED LOAN SETTLEMENT CHARGE : $______

III. OTHER REQUIRED SETTLEMENT COSTS:

In addition to the GUARANTEED LOAN SETTLEMENT CHARGE , you are or may be required to pay advance mortgage, hazard and flood insurance premiums, and to establish escrow reserves at settlement. Some of these costs may vary depending on when your loan closes and how much insurance you are required to obtain. In addition, you may be required to pay a lock-in fee if and when you decide to lock in the conditional interest price. No lender required cost may be imposed on you at settlement that is not specifically itemized and estimated in this Section other than the Guaranteed Loan Settlement Charge (or items expressly excluded from such Guaranteed Loan Settlement Charge) as described in Section II.

A. Per Diem Interest (HUD-1 900 Series) $_____
Per Diem at $____________ @ ____ days with an
estimated settlement of ______________

B. Reserves/ Escrow, (if required) (1000) $_____

C. Hazard Insurance (900) $_____

D. Mortgage Insurance
Based on a loan-to-value ratio of ___% $_____

E. Flood Insurance $_____

F. Lock-in Fee $ _____

IV. OPTIONAL OWNER'S TITLE INSURANCE (1100)

[PROPERTY TAXES]

TOTAL ESTIMATED SETTLEMENT COSTS (SUM OF SEC. II and III: $________

V. ADDITIONAL LOAN TERMS

This loan does does not have a prepayment penalty.
This loan does does not have adjustable rate terms.
This loan does does not have a scheduled balloon payment.

VI. GUARANTEED MORTGAGE PACKAGE AGREEMENT

By signing, dating, and returning this GMPA to us within the time period specified in the first paragraph of this Agreement, together with the specified application-related fee, you and we will be contractually bound to the terms of this GMPA provided that you qualify for this mortgage based on your credit rating, the appraisal, and other appropriate criteria.**** We certify that if we do not fund loans, we have arrangements with one or more lenders to which our guaranteed mortgage packages are acceptable, subject to such lenders' underwriting and final approval of the loan.

Signature of Authorized Agent Date

Signature(s) of Borrower(s) Date

**** This offer does not constitute an application for credit as that phrase is defined under applicable federal law, unless and until you accept this offer.

Tab 5

Guaranteed Mortgage Package – Form HUD-1

A. **Settlement Statement**			**U.S. Department of Housing and Urban Development**
B. Type of Loan			
1. ☐ FHA 2. ☐ FmHA 3. ☐ Conv. Unions 4. ☐ VA 5. ☐ Conv. Ins.	6. File Number	7. Loan Number	8. Mortgage Insurance Case Number
C. Note: This form is furnished to give you a statement of actual settlement costs. Amounts paid to and by the settlement agent are shown. Items marked "(p.o.c.)" were paid outside the closing; they are shown here for informational purposes and are not included in the totals.			
D. Name & Address of Borrower	E. Name & Address of Seller	F. Name & Address of Lender	G. Name & Address of Packager
H. Property Location		I. Settlement Agent	
		Place of Settlement	J. Settlement Date

K. Summary of Borrower's Transaction		**L. Summary of Seller's Transactions**	
100. Gross Amount Due From Borrower		**400. Gross Amount Due to Seller**	
101. Contract Sales Price		401. Contract Sales Price	
102. Personal Property		402. Personal Property	
103. Settlement Charges to Borrower (Line 1400)		403.	
104.		404.	
105.		405.	
Adjustment for items paid by seller in advance		**Adjustments for items paid by seller in advance**	
106. City/town taxes to		406. City/town taxes to	
107. County taxes to		407. County taxes to	
108. Assessments to		408. Assessments to	
109.		409.	
110.		410.	
111.		411.	
112.		412.	
120. Gross Amount Due From Borrower		**420. Gross Amount Due to Seller**	
200. Amounts Paid By or In Behalf of Borrower		**500. Reductions in Amount Due to Seller**	
201. Deposit or earnest money		501. Excess deposit (see instructions)	
202. Principal amount of new loan(s)		502. Settlement charges to seller (line 1400)	
203. Existing loan(s) taken subject to		503. Existing loan(s) taken subject to	
204.		504. Payoff of first mortgage loan	
205.		505. Payoff of second mortgage loan	
206.		506.	
207.		507.	
208.		508.	
209.		509.	
Adjustments for items unpaid by seller		**Adjustments for items paid by seller**	
210. City/town taxes to		510. City/town taxes to	
211. County taxes to		511. County taxes to	
212. Assessments to		512. Assessments to	
213.		513.	
214.		514.	
215.		515.	
216.		516.	
217.		517.	
218.		518.	
219.		519.	

220. Total Paid By/For Borrower		**520. Total Reduction Amount Due Seller**	
300. Cash at Settlement From/To Borrower		**600. Cash At Settlement To/From Seller**	
301. Gross Amount due from borrower (line 120)		601. Gross amount due to seller (line 420)	
302. Less amounts paid by/for borrower (line 120)		602. Less Reduction in amt. due seller (line 520)	
303. Cash ☐ From ☐ to Borrower		603. Cash ☐ To ☐ From Seller	

	Paid From Borrower's Funds at Settlement	Paid From Seller's Funds at Settlement
M. PURCHASE SETTLEMENT CHARGES		
700. Total Sales/Broker's Commission based on price $ @ %		
Division of Commission (line 700) as follows:		
701. $ to		
702. $ to		
703. Commission paid at Settlement		
704.		
1100. Title Charges Unrelated to Mortgage		
1101. Settlement or closing fee To		
1102. Owner's Title Insurance binder To		
1103. Notary fees for Deed To		
1104. Borrower's Attorney fees To		
(includes above item numbers:)		
1105. Seller's Attorney Fees To		
(includes above item numbers:)		
1106. Owner's title insurance		
1200. Government Recording and Transfer Charges Unrelated to Mortgage		
1201. Recording fees: Deed $ Releases of Prior Lien $		
1202. City/county tax stamps on Deed		
1203. State tax/stamps on Deed		
1300. Additional Settlement Charges Unrelated to Mortgage		
1301. Survey to		
1302. Pest inspection to		
1303.		
1304.		
1305. Total Purchase Settlement Charges		

N. LOAN SETTLEMENT CHARGES		
801. Guaranteed Loan Settlement Charge		
802. Loan Discount (or Credit) %		
901. Interest to @ per day		
902. Mortgage Insurance Premium for __ months to		
903. Hazard Insurance Premium for __ months to		
904. Flood Insurance Premium for __ months to		
1000. Reserves Deposited with Lender		
1001. Lock-In Fee		
1002.		
1003.		
1004.		
1005. Total Loan Settlement Charges		

1400. Total Settlement Charges (enter on lines 103K and 502L)		

Tab 6

Sample Mortgage Broker Fee Agreement

Mortgage Broker Fee Agreement

In the following: I or me = Applicant; You = Mortgage Broker.

Mortgage Brokerage Assistance. You are duly authorized and prepared to assist me in arranging mortgage financing for my home, and you agree to provide such assistance, as set forth below.

Amount of Broker Compensation. I understand that, as compensation for the goods, services and facilities you provide, your total mortgage broker compensation from all sources will not exceed:

[$_______________.

and / or [*specify which*]

[______________________ point(s)] (one points equals 1 percent of the original principal balance of the actual mortgage loan obtained.)

Method of Broker Compensation Payment. I understand that I may have a choice as to how your compensation is paid. Depending on such factors as my financial circumstances, whether I qualify for a loan and/or whether a loan program is available:

- I may pay your compensation for the services you provide out of my pocket directly.
- If I want to lower the amount I compensate you out of my pocket directly:
  - ➢ I may have the lender pay some or all of your compensation, in which case the lender will charge me a higher interest rate which could result in higher monthly payments; and/or
  - ➢ I may use the proceeds of the loan to pay some or all of your compensation, in which case I will be obligated to repay that amount with interest over the term of the loan.

I understand that I should discuss with you in further detail the specific options available to me to pay for your compensation, including the impact of each such option on the amount of cash I must bring to the closing, my interest rate, loan amount and monthly payments.

Nature of the Relationship. [Choose appropriate text] [Independent Contractor – I understand that in connection with this Agreement, you are not acting as my agent. You are also not acting as the lender's agent. Although you seek to assist me in meeting my financial needs, you may not make available the products of all lenders or investors in the market or the lowest prices or best terms available in the market.] [Borrower Agent – I understand that in connection with this Agreement and any mortgage loan you arrange for me, you are acting as my agent. You are not acting as the lender's agent. Although you seek to assist me in meeting my financial needs, you do not distribute the products of all lenders or investors in the market and cannot guarantee the lowest prices or best terms available in the market.] [Lender's Agent – In assisting to arrange financing for my home, I understand that you are not my agent and that you are acting as the agent of the lender.]

Termination. This Agreement will continue until one of the following events occurs:

- I fail to receive loan approval;

- My loan closes;
- I terminate this Agreement;
- You and I enter into a new Mortgage Broker Fee Agreement; or
- _________ days expire from the date of this Agreement without any of the foregoing occurring.

Mortgage Broker Fee and Disclosure Acknowledgement

By signing below, I/we understand and agree to the terms of this Agreement. The contractual obligation to comply with this Agreement rests solely with the mortgage broker and the applicants signing below. No other entity shall be liable for any misrepresentation or non-performance of the mortgage broker's obligations under this Agreement, or the mortgage broker's collection of compensation in excess of the maximum compensation stated herein.

Signing this Agreement does not obligate me to obtain a mortgage loan through you, nor does it prevent me from shopping for mortgage loans with any other mortgage broker or lender. his Agreement does not constitute a loan commitment or otherwise indicate mortgage loan approval.

I acknowledge that you and any lender that makes a loan to me is relying upon this Agreement and upon my statement that I actually understand your role in the transaction and how you will be paid.

* Applicant________________________________ Date________________

* Applicant________________________________ Date________________

____
Mortgage Broker's Signature
Mortgage Broker's License No. (where applicable) ________________________

Statement of John Courson

President & CEO
Central Pacific Mortgage Company
Folsom, California

on behalf of

Mortgage Bankers Association of America

before the

Committee on Financial Services

Subcommittee on Housing and Community Opportunity

U.S. House of Representatives

Hearing on

HUD's RESPA Reform Proposal

February 25, 2003

Good morning Mr. Chairman and members of the Committee. My name is John Courson, and I am President and CEO of Central Pacific Mortgage Company, headquartered in Folsom, CA. I am also Chairman of the Mortgage Bankers Association of America (MBA),[1] and it is in that capacity that I appear before you today.

I thank you for inviting MBA to form part of the important discussions regarding regulatory reform of the Real Estate Settlement Procedures Act ("RESPA"). This regulatory reform initiative, as set forth in HUD's recently issued proposed rule entitled "*Simplifying and Improving the Process of Obtaining Mortgages To Reduce Settlement Costs to Consumers*,"[2] will have far-reaching import for our industry and on the American consumer.

I want to begin my presentation by stating that we strongly support Secretary Martinez in his initiatives to simplify and improve the mortgage process, and we believe that the Proposed Rule is a major step forward for both consumers and the industry. MBA commends the Secretary on issuing this sweeping proposal. The issues and controversies implicated by RESPA, a broad-reaching, 29-year

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[1] MBA is the premier trade association representing the real estate finance industry. Headquartered in Washington, D.C., the association works to ensure the continued strength of the nation's residential and commercial real estate markets, to expand homeownership prospects through increased affordability, and to extend access to affordable housing to all Americans. MBA promotes fair and ethical lending practices and fosters excellence and technical know-how among real estate professionals through a wide range of educational programs and technical publications. Its membership of approximately 2,600 companies includes all elements of real estate finance: mortgage companies, mortgage brokers, commercial banks, thrifts, life insurance companies and others in the mortgage lending field.
[2] 67 F.R. 49134 ("Proposed Rule").

old statute, are complex and politically thorny. Undaunted, Secretary Martinez has recognized that the mortgage process has become much too complex and that there currently exists an urgent need to thoroughly reform the process in order to ensure the objectives of clear disclosures and consumer protection in the mortgage shopping process. The sheer scope of HUD's proposal demonstrates a great deal of leadership and courage by the Secretary. This reform initiative also demonstrates foresight on the part of HUD, as it brings real solutions to the table, and challenges us all to come together and reach agreement on fixing a mortgage disclosure system that has become increasingly complex and burdensome for all the parties involved.

MBA Position

MBA has consistently called out for the need to enact fundamental reforms to the bewildering and confusing mortgage shopping process. MBA has been a constant partner in discussions with government and consumer groups to craft workable methods to simplify and improve the mortgage process.

MBA sees HUD's Proposed Rule as a unique opportunity to effectuate large portions of long-discussed improvements to the mortgage process. As can be expected with any far-reaching project to improve and innovate existing systems, we believe that there are a number of technical issues that still require attention and resolution by HUD. Notwithstanding these details, we want to make clear to the Committee that MBA fully embraces the more important concepts of reform advanced by HUD's proposed rule. MBA believes that, if properly structured, HUD's "Guaranteed Mortgage Package" system will improve and simplify disclosures, foster market competition, and strongly enhance protections for all consumers.

The Current System

To properly appreciate the benefits of the reform proposals now advanced by Secretary Martinez, it is fundamental to understand how the current home mortgage disclosure system operates and why it has been criticized as flawed and ineffective in adequately protecting mortgage shoppers.

Disclosures

The Congressional intent in enacting RESPA was to protect consumers from unnecessarily high settlement costs by affording them with greater and more timely information regarding the nature and costs of the settlement process, and by prohibiting certain business practices. The statute sets out to achieve these goals through two principal disclosures—the good faith estimate of settlement costs (GFE) and the settlement statement (HUD-1). The GFE provides consumers with an itemized estimate of the costs the consumer will be required to pay at closing. This disclosure, containing such items as fees for origination, surveys, appraisal, credit report, etc., must be given to consumers within three days of application for a mortgage loan. The second key disclosure, the HUD-1, is provided to the consumer at closing, and lists all actual costs paid at, or in connection with, the settlement.

From a consumer's perspective, these forms may be effective in alerting them as to the generally anticipated costs they will have to incur at settlement, but the disclosures fall short of providing them with reliable figures that they need to effectively shop the market. As its name implies, the "good faith estimate" requires that cost disclosures to consumers be made in good faith, and that they bear a "reasonable relationship" to actual charges. RESPA does not impose any liability on the creditor for an inaccurate or incomplete estimate, nor for failing to provide one at all. It is important to understand the reality of the current law—the figures disclosed on the GFE, the key disclosure that consumers use to shop for settlement services, are neither firm nor guaranteed. If a consumer discovers that that the cost estimates they received at application differ significantly from the final HUD-1 figures, they have no redress or federal remedy to address the inaccuracies.

MBA believes that this legal structure is entirely inappropriate for both consumers and industry. Consumers that shop the market for the best prices available can never be assured of the actual costs at settlement. This system also provides little incentive for creditors and others to increase accuracy or incur risks in order to ensure such accuracy. In fact, it is the unscrupulous actors that benefit, as bait-and-switch tactics cannot be detected, and the intentional underestimating of costs and fees actually bears rewards in the competitive market place.

A further criticism of current disclosures centers on their complexity. Under existing regulations, the GFE and HUD-1 forms must separately itemize every single charge associated with closing. Though the intent is noble, this requirement creates a massively complex form that hurls disparate and obscure figures at consumers in a way that they cannot comprehend or effectively use to shop.[3]

From the industry's perspective, these disclosures are burdensome and expensive to administer. Not only are the forms costly to produce, but more importantly, they are subject to varying interpretations by different jurisdictions and regulatory entities. Creditors are always uncertain as to what degree of itemization is required, how certain costs are to be disclosed in instances where the services are out-sourced, and what line items to use in instances of non-traditional transactions that require special services. This is exacerbated by the fact that closing requirements vary across state lines, thereby causing disclosure requirements to vary in order to accommodate for such differences. Often, local

[3] For example, some of the fees required to be listed on the GFE may constitute costs that are already included and built into the loan's interest rate. Others may be fees that are dependent on the loan amount or price of the property.

jurisdictions create disclosure requirements that are in direct contradiction to express federal guidelines.

Section 8

Further difficulties arise in connection with the restrictions found under Section 8 of RESPA. This portion of the statute prohibits kickbacks, fee-splitting, fees for referrals of "settlement service business," and unearned fees, and imposes very heavy monetary and criminal penalties. MBA believes that the anti-steering provisions of Section 8 of RESPA serve very legitimate consumer protection purposes, as they shield home shoppers from improper influences that hamper shopping and competition. However, RESPA's Section 8 provisions are vague and subject to varying interpretations that impose barriers to cost-saving arrangements. For example, any attempt by lenders to negotiate for better prices with third-party settlement service providers, or efforts to regularize costs through average-cost pricing, could be deemed to constitute violations of Section 8.

I must note that all of the disclosure and legal complexities I describe here frequently lead to expensive and baseless class action litigation. Conflicting advisory opinions emanating from regulators can create classes of plaintiffs based on one or another of the varying interpretations. Special mortgage products that lower costs and benefit consumers create uncertainties under the ambiguous application of the RESPA statute. The Internet is now growing as the dominant medium for commerce, and yet the anti-kickback provisions of RESPA have not yet been clarified vis-à-vis online transactions. All these legal risks are menacing to industry, and generate massive legal and regulatory costs that can only be passed on to consumers through higher prices.

Need For Change

Although we can all agree that the American home finance system is recognized as the best and most efficient in the world, we cannot ignore the fact that consumer confusion persists and that the mortgage settlement process is bewildering to most home shoppers. The problems outlined above are real and have the effect of raising costs and trumping true competition in the market place. Worse still, in many instances, the confusion created by the current labyrinth of forms and disclosures allows unscrupulous actors to dupe and defraud even the most careful consumer. We believe, and repeat here today, that the scourge of "predatory lending" is in large part caused by the complex disclosure laws that allow dishonest players to perpetrate deception on unwary consumers.

Mr. Chairman, we can do better, and through this proposed rule, HUD has provided us with the blueprint from which to start our reform efforts.

HUD's Proposal

The Department's Proposed Rule, issued on July 19, 2002, contains far-reaching proposals that could fix virtually all the market and consumer problems I have identified above. The central element of HUD's proposal focuses on the creation of a carefully defined safe harbor that produces greater clarity and increased reliability for the shopping consumer. Under HUD's Proposed Rule, lenders and other settlement service providers would be allowed the option of offering applicants a "guaranteed" fee package in lieu of a GFE. This guarantee, dubbed the "Guaranteed Mortgage Package" ("GMP") under the proposal, would require a single lump-sum amount that represents the total of those costs expected to be incurred in connection with the originating, processing, underwriting and funding of that loan. As an important element of the GMP system, HUD is requiring that entities engaging in packaging offer to consumers, within 3 days of a loan application, an "interest rate guarantee," subject to change resulting only from a change in an "observable and verifiable index" or based on other appropriate data or means to ensure the guarantee. To encourage shopping, the proposal would not allow lenders to collect any application fees (prior to consumer acceptance of the GMP offer). Under the proposal, any person who assembles and offers such a package or whose services are included in such a package would be exempt from the restrictions and prohibitions of Section 8 of RESPA relating to referral fees, mark-ups, volume discounts, and fee splitting.

The Concept of "Packaging"

MBA believes, and has long advocated, that the "guaranteed fee package system" of the type set forth by HUD is the most effective way to achieve accurate disclosures for consumers. The effectiveness of this system is premised on the reality that consumers do not generally shop for individual settlement services, such as appraisal and credit reporting services. Rather, consumers shop for the mortgage loan, which is the central element that in turn requires the purchase of the other ancillary services. Since each lender has different loan products, and since each lender has different investors that impose different requirements pertaining to such services, these ancillary services can rarely be purchased independently from the mortgage loan. As they advance through the mortgage shopping process, consumers tend to focus only on the mortgage loan, and are therefore interested in the overall "price" of the loan itself rather than the individual price for those ancillary services performed for the benefit of the creditor or the ultimate investor.

The "packaging" system recognizes this reality, and constructs a system whereby the consumer is presented with a single price that includes all items required to close the loan. The "packaging" system streamlines cost disclosures to consumers by assembling practically all required closing costs under one single figure, thereby allowing consumers to better understand the overall cost of the loan transaction. Unlike the estimates provided under the GFE, the "package" price offered to consumers would be solid and guaranteed very early in the shopping process. This cost reliability allows consumers to shop the market and effectively compare total settlement service prices among various sources. In short, the "packaging" system engenders market competition by encouraging comparison-shopping, which in turn allows market forces to influence costs and reduce unnecessary fees and charges.

Under a "packaging" system, consumers would receive an up-front disclosure guaranteeing costs relating to settlement. Packaging entities would therefore have an incentive to attain the best prices available in order to ensure the competitiveness of their packages. In a competitive environment, any price reduction achieved by the packager will surely be passed on to consumers.

The "packaging" system envisions a system that is free from unnecessary legal entanglements in terms of deals and activities necessary to arrive at the lowest possible guaranteed fee package. For example, the concept of "packaging" would create market incentives whereby lenders and other entities will seek out third-party settlement service providers in order to enter into volume-based contracts and otherwise secure discounts from providers in order to ultimately produce much lower settlement costs for consumers. It is also envisions that lenders will be able to solidify prices for consumers by "averaging" costs over a large number of transactions. As set forth above, today, these types of activities pose real risks under the hazy rules of Section 8 of RESPA. Average-cost pricing and volume-based compensation could be deemed to constitute improper referral schemes or "overcharges," which some would interpret as being violative of current RESPA rules.

Not only do these current restrictions pose undue complexities and legal risk, but more importantly, they are outdated and unnecessary under a guaranteed cost system. Inside of the package of guaranteed costs, consumers are fully protected because engaging in certain activities prohibited under Section 8 of RESPA would only serve to inflate the total "package" price, which in turn, would lead consumers to reject inflated-priced products for lesser-priced alternatives. The "packaging" system creates, therefore, a self-enforcing disclosure regime that saves government resources, promotes competition, and facilitates market innovation. The protections afforded by Section 8 should, however, remain fully applicable outside of the "package" arrangement, as we believe that improper steering would continue to have deleterious effects on market competition and consumer choice.

The Proposed Rule

HUD's GMP proposal incorporates this competitive "packaging" system, along with all of its benefits, into the current RESPA regulatory structure. As noted above, the Proposed Rule would afford a Section 8 exemption for entities that are willing to offer simplified disclosures to consumers, which must set forth a guaranteed cost for those services required to close a mortgage loan, along with an assured interest rate quote on the loan.

MBA believes that HUD's proposed guaranteed fee package proposal goes a long way in resolving most of the shortcomings and market failures associated with RESPA's current disclosure system. Under the proposal, HUD would allow "packagers" to replace the current GFE forms with an alternative "Guaranteed Mortgage Package Agreement" disclosure that streamlines the cost disclosures and presents closing costs to consumers as a lump-sum, fixed number that can be easily compared with other packaged products. This disclosure is provided to the mortgage shopper free of charge and very early in the loan application process, thereby encouraging comparison-shopping.

More importantly, HUD's proposal would require that the lump-sum package cost be absolutely guaranteed three days after application. For numerous reasons, this represents a very significant consumer protection provision. First, it allows consumers to shop the market with the confidence that they are comparing actual, final figures. Since the guaranteed mortgage package price incorporates practically all costs required to close the loan, the consumer's comparison shopping will not be clouded or confused with meaningless numbers. In addition, the "Guaranteed Mortgage Package Agreement" empowers the consumer to easily detect misdisclosures and effectively enforce their rights and their benefits in the bargain. Unlike the current system that allows for variances between the GFE and the HUD-1, HUD's proposed system imposes a "zero" tolerance on the initial and final disclosures; a mere inspection and comparison between the initial disclosure and the closing statement will suffice to clearly expose whether the costs were improperly inflated. The streamlining also eases enforcement for government regulators, and will make it much tougher to defraud the public.

MBA also believes that HUD's proposals are a step in the right direction in terms of clarifying confusing legal standards that breed pointless class action litigation. The convoluted rules of Section 8 of RESPA are rendered obsolete by using free market forces to compress prices and allowing firm and reliable disclosures to serve as the consumer's shield of protection. Likewise, disclosure difficulties are resolved through a straightforward lump-sum disclosure that incorporates practically all transaction fees, without the complex distinctions that exist today.

Summary

To summarize, MBA believes that, with some adjustments, the guaranteed cost packaging proposal proposed by HUD is a viable system that is certain to result in broad consumer benefits. The certainty and reliability inherent in this system will provide sound consumer protections while sharply stimulating market competition. In terms of industry benefits, the proposed system will go a long way in clarifying difficult rules and regulations that pose unnecessary legal risks and serve to trump operational efficiencies that could streamline the mortgage process.

Addendum: Additional Recommendations

Although MBA embraces HUD's Guaranteed Mortgage Package proposals, we believe that HUD must clarify and revisit certain components of the Proposed Rule. MBA has filed lengthy comments with HUD, setting out these recommendations in detail. For the benefit of the subcommittee, I summarize them below—

1. Interest Rate "Guarantee"

In the Proposed Rule, HUD is proposing that entities engaging in packaging offer to consumers, within 3 days of a loan application, an "interest rate guarantee, subject to change (prior to borrower lock-in) resulting only from a change in an observable and verifiable index or based on other appropriate data or means to ensure the guarantee." Through this requirement, HUD seeks to ensure that the rate of the loan does not vary after the borrower commits to a packager for reasons other than an increase in the cost of funds. The objective of the interest rate disclosure proposal, as articulated by HUD, is to protect against an increase in the packager's compensation through changes in the rate portion of the price quote.

Although MBA fully supports the Department's objectives with regards to the "Interest Rate Guarantee," we point out that any such regulatory plan must take into account that interest rate movements are set by open market forces that are not under any one lender's control. It must also be recognized that loan pricing is not exclusively influenced, nor fully measured, solely by the movement of any one index. Indeed, any index, even if applicable to pricing a mortgage product, may be only one in a number of components used to determine the ultimate price of a loan. Factors other than "interest rate index" fluctuations that would affect pricing include internal operating costs, product availability, capped investor commitments on particular loan programs, warehouse-line capacity and general capacity. In light of the unpredictability and shifting nature of the factors that affect loan pricing, our members believe that the protections sought by HUD can be afforded only under very specific conditions that allow financial institutions to effectively protect against financial risk. These carefully circumscribed conditions must be incorporated into any final rule. They are as follows—

- GMP interest rate "guarantee" should be renamed to reflect more accurately the nature of the disclosure.
- Retain the current definition of "application" under the RESPA regulations.
- Limit the post-disclosure shopping period to 5 days (or any additional period as determined only by the individual lender).

- Once the consumer accepts the GMP offer and "locks" the rate, the disclosed interest rate quote (subject to the index) is good only for as long as the duration of the "lock-in" period.
- GMP disclosure must list the specific loan product, and the "guarantee" would be applicable only to the specified product.
- Lenders must have full authority to select the appropriate rate "index".
- Lenders must have full authority to select different "indices" for different loan products.
- Lenders must have full authority in setting the "spreads" applicable to the interest rate quotes.
- Lenders must be afforded the option of regularly publishing their rates as an alternative means of complying with the GMP rate quote requirement.

2. Modifications to Good Faith Estimate

For numerous reasons, HUD should delay the implementation of the Revised Good Faith Estimate ("GFE") proposals. As currently drafted these proposals are extremely complex and in our opinion, unnecessary in light of the extraordinary pro-consumer reforms advanced under the GMPA proposal. We are, therefore, asking that changes to the GFE be delayed until after the market has had an opportunity to accommodate the packaging reforms. After a reasonable period of implementation, HUD should revisit the need for any additional changes to the current GFE system

Notwithstanding our position to delay the implementation of the Revised GFE, MBA agrees with HUD that confusion regarding mortgage broker compensation continues to be a vexing issue for consumers and that greater disclosure regarding broker fees may be necessary. MBA therefore recommends that HUD adopt the Mortgage Broker Fee Agreement Disclosure already introduced by a coalition of trade associations to HUD a few months ago, with the attendant exemption for brokers and lenders from Section 8 scrutiny. This additional disclosure would achieve HUD's goals of full disclosure and greater consumer education.

3. Preemption

HUD should clearly announce its intent to seek preemption of state law that conflicts with the provisions established by any final rule. HUD should also take immediate action to facilitate this preemption of state law.

4. Conflicts With Federal Laws

MBA has recommended that HUD address the conflicts with other Federal laws that will result from this proposed rule. Particularly, HUD should engage the Federal Reserve Board on the implications this Proposed Rule will have with regard to the Truth in Lending Act and Regulation Z. The technical requirements contained in TILA, give rise to several conflicts between that law and the proposed regulations. In light of certain itemizations and "Finance Charge" calculations mandated by TILA, lenders could potentially lose the flexibility that is necessary to accomplish the goals of the GMPA. Since some of these requirements have a statutory basis, Congressional action may be required to ultimately resolve this matter.

National Association of Mortgage Brokers

Prepared Testimony of Neill Fendly, Government Affairs Chair & Past President

National Association of Mortgage Brokers

on

HUD's Proposal to Reform RESPA

before the

Subcommittee on Housing and Community Opportunity

Committee on Financial Services

U.S. House of Representatives

Tuesday, February 25, 2003 RHOB 2128

Chairman Ney, Ranking Member Waters, Members of this Subcommittee, I am Neill Fendly, the current Government Affairs Chair and Past President of the National Association of Mortgage Brokers (NAMB), the nation's largest organization exclusively representing the interests of the mortgage brokerage industry. We appreciate the opportunity to address the Subcommittee today on behalf of the nation's mortgage brokers on the Department of Housing and Urban Development's (HUD) recently proposed rule (Proposed Rule) amending Regulation X, the implementing regulation for the Real Estate Settlement Procedures Act (RESPA).

NAMB has more than 14,000 members and 46 state affiliates nationwide. NAMB provides education, certification, industry representation, and publications for the mortgage broker industry. NAMB members subscribe to a strict code of ethics and a set of best business practices that promote integrity, confidentiality, and above all, the highest levels of professional service to the consumer.

In short, NAMB believes that HUD's Proposed Rule would limit consumer choice and access to credit, is unworkable in the real world, and would increase the regulatory burden on small business. In addition, NAMB finds the economic analysis and regulatory burden documents prepared by HUD to be flawed, inconsistent and dubious at best.[1] HUD has received over 40,000 comment letters expressing grave concern on the merits of HUD's Proposed Rule. NAMB believes the Proposed Rule violates the Unfunded Mandates Reform Act,[2] as well as President Bush's recent Executive Order[3] to reduce regulatory burden on small business. Our testimony today centers on the Proposed Rule's negative impact on consumers and disproportionate impact on small business, especially mortgage brokers.

Who We Are and What We Do

A mortgage broker is an independent real estate financing professional who specializes in the origination of residential and/or commercial mortgages. A mortgage broker is also an independent contractor who markets and originates loans offered by multiple wholesale lenders. As a result, mortgage brokers offer consumers more choices in loan programs and products than a traditional mortgage lender. Mortgage brokers also offer consumers superior expertise and assistance in getting through the tedious and complicated loan process. Mortgage brokers also provide lenders a nationwide product distribution channel that is much less expensive than traditional lender retail branch operations (bricks and mortar).

Mortgage brokers serve the role as advisor, credit counselor, underwriter, and personal contact to the consumer. Mortgage brokers often originate loans for "difficult borrowers," those who are credit challenged, have income that is difficult to document, or are first time homebuyers. Mortgage brokers spend the time with these applicants, working together with them through credit problems, assisting those having no credit histories, and helping those individuals finance the purchase of their home.

Mortgage brokers are typically small businesses who operate in the communities in which they live. They are vital members of these communities, often operating in areas where traditional mortgage lenders may not have branch offices, such as rural communities. Were it not for mortgage brokers, many of these areas would be underserved and the dream of homeownership for these communities would not be fulfilled.

A mortgage broker does not simply press a few keys to provide the consumer with a mortgage loan. Nor are mortgage loans akin to products that can be picked from a shelf and paid for at checkout. Mortgage brokers perform a vital and unique role in assisting consumers in obtaining a mortgage loan. Indeed, this is why mortgage brokers originate more than 60% of all residential mortgages.[4]

In light of our role in placing families in homes, NAMB has great concern that HUD's Proposed Rule amending Regulation X will not serve to protect consumers but will instead further complicate the real estate settlement process and confuse the homebuyer. Introducing arbitrary and artificial price capping features and disclosure methods as set forth in HUD's Proposed Rule,

[1] *See* Attachment 1, "Discrepancies with HUD's Economic Analysis."
[2] 2 U.S.C. 1531 *et al.*
[3] Executive Order 13272, August 13, 2002.
[4] Prepared Statement of Mr. David Olson, President, Olson Research, U.S. Senate Committee on Banking, Housing, and Urban Affairs Hearing on "Predatory Lending Practices: Abusive Uses of YSPs," January 8, 2002.

could adversely impact the housing market by reducing access to credit as well as driving up costs for consumers.

First and foremost HUD's Proposed Rule recharacterizes the definition of yield spread premium which contradicts HUD's own Statements of Policy 1999-1 and 2001-1. Such a change creates an ambiguity in the marketplace that not only confuses the borrower, but also will lead to a new round of class action litigation. NAMB also believes HUD's Proposed Rule creates an unlevel playing field since it requires that indirect compensation **for mortgage brokers only** must be disclosed as a lender payment to the borrower. We are disappointed that HUD acknowledges that the Proposed Rule "results in different treatment of compensation in loans originated by lenders and those originated by mortgage brokers."[5] In addition, the burden associated with the Proposed Rule is staggering and as recognized by HUD, falls disproportionately on small business.[6] NAMB also believes that HUD's Proposed Rule's provisions on packaging are anti-competitive and will result in the largest multi-billion dollar originators dominating the mortgage industry to the detriment of consumers.

NAMB is extremely concerned that this Proposed Rule, if implemented as written, will have a dramatic impact on the cost of credit for consumers as well as small business, the mortgage financing industry and the mortgage broker industry in particular. We believe such a sweeping rewrite of RESPA at this point in time is not prudent for anyone – the homebuyer, the mortgage broker or especially, the economy.

I. NAMB's Concerns with HUD's Proposed Rule in Connection with the Enhanced Good Faith Estimate

A. Characterization of Yield Spread Premiums as a "Lender Payment to the Borrower"

HUD's Proposed Rule recharacterizes the definition of yield spread premiums as a "lender payment to the borrower for a higher interest rate." This characterization creates unintended consequences and provides less clarity to consumers than as presently disclosed. The recharacterization is also inconsistent with HUD's Statements of Policy 1999-1 and 2001-1, in which HUD states that a yield spread premium is a payment for "goods, facilities or services furnished or performed," ***for the lender*** [emphasis added] as well as the borrower. In HUD's Statement of Policy 1999-1, HUD stated that "the Department recognized that some of the goods or facilities actually furnished or services actually performed by the broker in originating a loan are 'for' the lender and other goods or facilities actually furnished or services actually performed are 'for' the borrower."[7] HUD reemphasized these statements in its Statement of Policy 2001-1.[8] Further, in the Proposed Rule, HUD stated that "as retailers, brokers also provide the borrower **and lender** [emphasis added] with goods and facilities such as reports, equipment, and office

[5] Real Estate Settlement Procedures Act, 67 Fed. Reg. 49,134, 49,148 (July 29, 2002).
[6] "Economic Analysis and Initial Regulatory Flexibility Analysis for RESPA Proposed Rule to Simplify and Improve the Process of Obtaining Mortgages to Reduce Settlement Costs to Consumers," U.S. Department of Housing and Urban Development, Office of Policy Development and Research, July 2002, p. vii.
[7] Real Estate Settlement Procedures Act, Statement of Policy 1999-1, 64 Fed. Reg. 10,080, 10,086 (March 1, 1999).
[8] Real Estate Settlement Procedures Act, Statement of Policy 2001-1, 66 Fed. Reg. 53,052, 53,055 (October 18, 2001).

space to carry out retail functions."[9] HUD further stated that "mortgage brokers essentially provide retail lending services."[10]

Yield spread premiums are used to pay the costs incurred in connection with a mortgage broker's business. Mortgage lenders save millions of dollars in facilities and employee costs by originating loans through mortgage brokers. However, these costs do not entirely disappear for the mortgage broker– a mortgage broker must pay for its employees, office facilities, and basic operations (computers, software and other such information). By characterizing the yield spread premium as a "lender payment to the borrower," HUD has discounted any payment to the broker by the lender for goods or facilities actually furnished or services actually performed for the lender.

HUD's recharacterization of the definition of yield spread premium limits consumer choice and renders mortgage brokers unable to compete with lenders. It also does not achieve the goal of simplification, but instead confuses the consumer on exactly how indirect broker compensation works and how it can benefit the consumer.

i. The Manner of Disclosure Further Unlevels the Playing Field Creating a Regulatory (*i.e.* artificial) Competitive Disadvantages for Mortgage Brokers

The Proposed Rule further unlevels the playing field in singling out indirect compensation to mortgage brokers only. By regulating that mortgage brokers must include the yield spread premium in the *calculation* of Net Loan Origination Charge, but not including the same of all originators, HUD is complicating the real estate settlement process because the consumer is unable to perform a true "apples to apples" comparison of the cost of the mortgage. This is contrary to HUD's goal of simplifying and improving the mortgage loan process.

Mortgage lenders also receive indirect compensation when a loan is sold on the secondary market. However, due to an exemption created by HUD through the regulatory process,[11] these transactions are exempt from, among other things, the disclosure requirements for yield spread premiums. This creates an unlevel playing field for mortgage brokers. HUD has even stated that "lenders are able to offer loans with low or no up-front costs required at closing by charging higher interest rates and recouping the costs by selling the loans into the secondary market for a price representing the difference between the interest rate on the loan and the par, or market, interest rate."[12] This is called a service release premium (SRP). The sale of such a loan achieves the same purpose as the yield spread premium does on a loan originated by a broker. Under HUD's Proposed Rule traditional lenders will continue to receive this indirect compensation but will not be required to disclose it in the marketplace.

[9] Real Estate Settlement Procedures Act, 67 Fed. Reg., 49,134, 49,140 (July 29, 2002).
[10] *Id.*
[11] 24 C.F.R. § 3500.5(7).
[12] Real Estate Settlement Procedures Act, Statement of Policy 2001-1, 66 Fed. Reg. 53,052, 53,056 (October 18, 2001).

If the proposed characterization of yield spread premiums is implemented, mortgage brokers will not be able to advertise certain mortgage loans and remain competitive. For example, a mortgage *broker* who makes a "no point" mortgage loan at 7% interest rate on a $100,000 loan, but collects a $1,000 yield spread premium, must advertise that this is a one-point mortgage loan. A mortgage *lender*, who originates a $100,000 mortgage loan at a 7% interest rate, but collects $1,000 in compensation when the loan is sold, can advertise a "no-point" mortgage loan. These are the exact same loans with the exact same costs to the consumer. However, due to a federally regulated mandate (*i.e.* artificial) the mortgage broker appears more expensive as he or she must advertise that this is a one-point mortgage loan.

In addition, by including a mortgage broker's indirect compensation in the calculation of the Net Loan Origination Charge, consumers will suffer a loss of available credit as many mortgage brokers will no longer be able to originate FHA and VA-insured mortgage loans. This is because direct originator compensation on these loans is limited to 1% of the loan amount in connection with FHA-insured loans, and direct originator compensation on VA-insured mortgage loans is limited to 1% of the total loan amount or closing costs. In characterizing yield spread premiums as a lender payment to the borrower, indirect compensation to a broker is artificially transformed into direct compensation and thus subject to the cap. This will impact many first time homebuyers who rely on FHA and VA-insured mortgage loans for their loan down payment requirements and force these consumers into subprime loans. This is significant as approximately 31% of all FHA-insured loans are originated by mortgage brokers.[13]

The federal government should not be in the business of picking winners and losers in the marketplace. Nor should a regulator be able to dictate the playing field by regulatory fiat. The HUD Proposed Rule does both.

ii. HUD's Recharacterization is Confusing to Consumers and Will Lead to a New Round of Class Action Lawsuits

Unfortunately, the stark reality of business is that any increase in the amount of money spent in defending any lawsuits will ultimately be passed through to the consumer in the form of higher costs for originating a mortgage loan. HUD's proposed recharacterization of yield spread premiums as a "lender payment to the borrower" will create confusion for consumers which will lead them to the question – "where is my check?" A borrower claiming fraud, when no check appears, will seek counsel to litigate the issue. HUD's recharacterization creates a clear opportunity for a new round of class action lawsuits.

The issues relative to the payment of yield spread premiums have been scrutinized a great deal by the courts. The courts, however, have relied on HUD's 1999-1 and 2001-1 Statements of Policy in determining the legality of yield spread premiums. To date, HUD's Statements of Policy 1999-1 and 2001-1 have provided structured guidance to the courts by eliminating the ambiguity relating to the legality of lender payments to mortgage brokers. They have provided certainty to the marketplace, which in effect, has helped to curb Section 8 class action lawsuits.

[13] Letter from Engram A. Lloyd, Director, Philadelphia Homeownership Center, Department of Housing and Urban Development, to Paul H. Scheiber, Blank Rome Comiskey & McCauley LLP on 8/12/2002.

However, HUD's proposed recharacterization of yield spread premiums in the Proposed Rule will only spur another round of litigation and costs associated with such litigation will eventually be passed on to the consumer. Any increase in costs to the consumer for mortgage financing can lead to a decrease in homeownership as affordable mortgage financing becomes too expensive for families to handle. NAMB fears this very real and distinct threat of liability.

B. Other Concerns with HUD's Proposed Good Faith Estimate

Please note that NAMB has other concerns with the Proposed Rule's Good Faith Estimate requirements. Currently, RESPA requires that a consumer be provided "a good faith estimate of the amount or range of charges for specific settlement services that the borrower is likely to incur in connection with the settlement" of a mortgage loan in a manner "prescribed by the Secretary."[14] The Proposed Rule would require originators to provide consumers with a *guarantee* of certain costs within three business (3) days of application. [15] HUD makes a rather large leap from requiring a "good faith estimate" disclosure of costs, as mandated by Congress, to a *guarantee* of many costs.

Mandating a guarantee of third party costs, at this early stage, is unreasonable. Loan originators cannot predict every cost of every loan. This is because every home is unique and every mortgage transaction is unique. Consider when a wholesale lender requires additional comparisons on an appraisal, or when the underwriter requests another survey? Issues may surface with the property that are not foreseeable at application, such as the need for a survey, soil inspections in the case of earthquake zones, or pest inspections. The mortgage broker should not be held responsible for these unforeseen costs.

NAMB has other concerns for certain provisions of the Proposed Rule in connection with the enhanced "good faith estimate," but for the sake of brevity, refers the Subcommittee to NAMB's comment letter to HUD on the Proposed Rule. [16]

However, we think it is important to point out that NAMB has spent countless hours and resources to strengthen, simplify and clarify the disclosure of costs provided to consumers in advance of settlement. NAMB submitted an alternative disclosure form set forth in our comment letter that satisfies the objectives of HUD to simplify the mortgage process, but not at the expense of small business or to the detriment of consumers.[17] It will allow the consumer to perform a true "apples to apples" comparison of the cost of the mortgage while maintaining a more level playing field for mortgage originators.

[14] 12 U.S.C. § 2604(c).
[15] Real Estate Settlement Procedures Act, 67 Fed. Reg., 49,134, 49,159 (July 29, 2002).
[16] *See* Attachment 2, Comment Letter submitted by National Association of Mortgage Brokers, on the "Real Estate Settlement Procedures Act, Simplifying and Improving the Process for Obtaining Mortgages to Reduce Settlement Costs to Consumers," U.S. Department of Housing and Urban Development, FR-4727-P-01 (July 29, 2002).
[17] *Id.*

II. NAMB's Concerns with HUD's Proposed Rule with the Packaging of Settlement Services

The Proposed Rule also sets up a new process for originating mortgages called the Guaranteed Mortgage Package Agreement. Created by regulatory fiat, this regime requires an originator to offer a guaranteed mortgage package (mortgage, third party settlement services and closing costs) for a set price. The small business owner is going to be disadvantaged in the marketplace because he or she does not have the bargaining power to enter into volume-based contracts with vendors. The end result will be additional consolidation in the mortgage industry at the expense of small business. This burden will fall disproportionately on small business and is even articulated by HUD – "$3.5 billion of the $6.3 billion in transfers to borrowers comes from small originators ($2.2 billion) such as small brokers and small settlement service providers ($1.3 billion)."[18]

NAMB believes that mortgage brokers, as small businesses, will be greatly disadvantaged by the "regulatory driven packaging" (as opposed to market driven packaging) of settlement services.[19] Mortgage brokers, as small businesses,[20] do not have the bargaining power to enter into volume-based discounts with third party settlement service providers, as do larger entities. Under the Proposed Rule, many mortgage brokers would not be able to compete with the larger entities and will be forced out of business, or become an agent for one lender or two utilizing their packages, or utilize the enhanced good faith estimate approach, which could also disadvantage mortgage brokers. This will force mortgage brokers to lose their autonomy and limit their ability to offer consumers the choice of a wide array of products and services. This impact will be passed through to the consumers in the form of higher costs and less consumer choice.

Further, the packaging of settlement services is occurring today. Thus, the removal of regulatory barriers is not necessary to allow packaging of settlement services; rather, exemption from Section 8 liability creates an incentive for entities to offer packages. While HUD contends that packaging will decrease a consumer's settlement costs as competition drives these prices down,[21] it could also work to drive prices up as packagers can "up charge" costs. HUD's longstanding prohibition against the "up charging" of third party settlement costs will cease to exist only for

[18] "Economic Analysis and Initial Regulatory Flexibility Analysis for RESPA Proposed Rule to Simplify and Improve the Process of Obtaining Mortgages to Reduce Settlement Costs to Consumers," U.S. Department of Housing and Urban Development, Office of Policy Development and Research, July 2002, p. vii.

[19] Recent news articles have cited a decline in small business hiring, "creating another headwind for the nation's stubbornly sluggish economy recovery." *Small-business Hiring Dip Slows Recovery*, Ariz. Republic, Oct. 25, 2002, at D-1. Further, an article cites that "small businesses make up 98 percent of all enterprises in the nation and create about 65 percent of jobs." *Id.*

[20] The majority of mortgage brokers are small businesses. The Economic Analysis cites to a study in which it stated that most mortgage broker firms consist of one office and five employees (including the owner). "Economic Analysis and Initial Regulatory Flexibility Analysis for RESPA Proposed Rule to Simplify and Improve the Process of Obtaining Mortgages to Reduce Settlement Costs to Consumers," U.S. Department of Housing and Urban Development, Office of Policy Development and Research, July 2002, p. 12. Further more, this study stated that it found "brokers as low-cost, highly competitive firms, vigorously competing with one another and with little opportunity to earn above-normal profits." *Id.*

[21] "Economic Analysis," p. vii.

those who package. Those who choose to operate under the enhanced good faith estimate will still be subject to this prohibition.

NAMB also believes that there are many unworkable provisions in HUD's Proposed Rule in connection with packaging. These provisions include, among others, the failure in allowing all originators to package, providing a index for consumers to track their interest rate, allowing a consumer thirty (30) days to shop for a loan while the package is available, providing no itemization of costs that are in the package, and allowing the package to remain viable indefinitely, after acceptance.

III. The Proposed Rule Should Not Provide Additional Barriers for Minority Homeownership

President Bush and Secretary Martinez have been very vocal in their goal of increasing minority homeownership. Minority homeownership has recently been on the rise; in a press release dated April 24, 2002, the U.S. Census Bureau released data that showed that homeownership among Hispanics rose substantially to 46 percent.[22] However, as noted in other press releases, a Bush Administration analysis showed that "a large gap still exists between minority and white households."[23] The analysis showed that "since 1994, when the black homeownership rate was 27.5 percentage points below the rate of whites and the Hispanic rate was 28.8 percentage points below, only small gains have been made."[24] The analysis further showed that "by 2001 the gap had been reduced by just 1.6 percentage points for African Americans and 1.8 percentage points for Hispanic households."[25]

HUD's analysis identified several barriers for homeownership: "(i) lack of capital for the down payment and closing costs, often the single greatest barrier to homeownership; (ii) lack of access to credit and poor credit histories, which means more minority families are rejected for a mortgage loan or given loans with high interest rates; (iii) lack of understanding and information about the homebuying process, especially for families for whom English is a second language;" and (iv) others.[26]

Mortgage brokers are the key to bridging the gap in minority homeownership. Mortgage brokers are integral members of their community and provide access to credit that most large lenders cannot. A recent study performed by Wholesale Access, a research, advisory and publishing company, on minority lending stated that two of the key findings of this research are: "(i) brokers reach more minorities than lenders; and (ii) the explanation for this is found in their locations, products and staffing."[27] Many of these communities would not have the availability of mortgage loans currently enjoyed today were it not for mortgage brokers, who originate more

[22] Press Release. Department of Housing and Urban Development, Homeownership Increase Among Hispanics (April 24, 2002) (on www.hud.gov).
[23] News Release. Department of Housing and Urban Development, New HUD Report Identifies Barriers to Minority Homeownership, Outlines Bush Administration Actions to Overcome Them (June 17, 2002) (on www.hud.gov).
[24] *Id.*
[25] *Id.*
[26] *Id.*
[27] Press Release. Wholesale Access, Study of Minority Lending Completed, (Sept. 24, 2002) (on www.wholesaleaccess.com).

than 60% of all mortgage loans.[28] Any rule implemented by HUD should not impact the ability of mortgage brokers to assist minorities in obtaining homeownership.

IV. HUD's Economic Impact Analysis is Flawed, Inconsistent and Incomplete

NAMB finds HUD's economic analysis flawed and inconsistent. NAMB believes that further analysis is necessary to ensure that the numbers professed in the analysis bear out the impact any portion of the Proposed Rule will have in the marketplace. Conceiving, constructing and implementing a rule based on flawed, inaccurate and incomplete economic analysis will - by definition - lead to a flawed and incomplete rule that can cause great potential harm to the housing market. One cannot build a house without a solid foundation. This rule is not built on the solid foundation of market realities, but instead a fundamental misunderstanding of such realities. Basing the Proposed Rule on flawed economic analysis will result in a flawed final rule that harms consumers and could have devastating repercussions in a $2 trillion housing market.

Below, NAMB cites several inconsistencies between the information in the Economic Analysis and HUD's Paperwork Reduction Act Submissions to the Office of Management and Budget (OMB). Greater analysis is called for based upon the proposed dramatic impact the Proposed Rule, if finalized, will have on the mortgage industry for both industry and consumers. Finally, the disproportionate impact on small business necessitates further analysis under the Regulatory Flexibility Act.[29] Indeed, the Small Business Administration, Office of Advocacy, submitted a comment letter encouraging HUD to issue a revised initial regulatory flexibility analysis (IRFA) "that takes into consideration the comments of affected small entities and develops regulatory alternatives to achieve HUD's objectives while minimizing the impact on small business."[30]

NAMB believes HUD has significantly underestimated the regulatory burden of its Proposed Rule. Indeed, HUD's Paperwork Reduction Act Submissions to OMB states that annual responses for Good Faith Estimates (GFEs) is 11 million.[31] However, HUD's Economic Analysis and Initial Regulatory Flexibility Analysis, states that if the rule applied in the year 2002, it would impact 19.7 million applications.[32] This is significant because the submission to OMB underestimates the paperwork burden by at least 8.7 million GFEs and an additional $57 million.

In addition, HUD's Economic Analysis states that "originators and closing agents will have to expend some minimal effort in explaining to consumers the cross walk between the new streamlined GFE and the more detailed HUD-1."[33] However, this cost is not included in the

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[28] Prepared Statement of Mr. David Olson, President, Olson Research, U.S. Senate Committee on Banking, Housing, and Urban Affairs Hearing on "Predatory Lending Practices: Abusive Uses of YSPs," January 8, 2002.
[29] 5 U.S.C. § 601 *et seq.*
[30] *See* Attachment 3, Comment Letter submitted by the Office of Advocacy, Small Business Administration, on the "Real Estate Settlement Procedures Act, Simplifying and Improving the Process for Obtaining Mortgages to Reduce Settlement Costs to Consumers," U.S. Department of Housing and Urban Development, FR-4727-P-01 (July 29, 2002).
[31] *See* Attachment 4, "Supporting Statement for Paperwork Reduction Act Submissions," U.S. Department of Housing and Urban Development, August 2001, p. 5.
[32] "Economic Analysis," p. 9.
[33] *Id.* at p. 25.

OMB submission and the cost is not "minimal." NAMB believes a detailed and accurate estimate should be provided.

HUD states that the program change being mandated at HUD would increase burden to industry by 2,530,000 burden hours.[34] This is equal to 289 years. NAMB believes such a huge burden, by definition, will increase the cost of credit to consumers. NAMB also believes this anticipated burden triggers the Unfunded Mandates Reform Act and conflicts with President Bush's recent Executive Order to relieve the regulatory burden on, and protect, small business.[35]

The Economic Analysis states that $3.5 billion of the $6.3 billion (55%) in transfers to consumers will come from small businesses.[36] NAMB finds this very troubling in the sense that small business – particularly in the housing industry today – is one of the few pillars in this economy that has not fallen. NAMB is concerned that by arbitrarily reducing small business revenues, many will not be able to survive and will therefore reduce consumer choice and access to credit. HUD should ensure that the final regulation would not disproportionately jeopardize the small businessman currently trying to put people in homes.

This and other inconsistencies compel NAMB to ask whether HUD must undergo a more expansive and realistic review of the economic impact this rule will have on the industry, as well as small business, as mandated by the Regulatory Flexibility Act, the Paperwork Reduction Act, the Unfunded Mandates Reform Act, and President Bush's recent Executive Order to relieve the regulatory burden on, and protect, small business.

NAMB has attached a list of discrepancies with HUD's Economic Analysis to this testimony to highlight some of the flaws and inconsistencies.[37]

V. Conclusion

NAMB sincerely appreciates the opportunity to share our concerns with the Subcommittee on HUD's Proposed Rule to reform RESPA. We commend this Subcommittee for convening this hearing on this very important issue. NAMB is very concerned that if HUD proceeds to finalize the Proposed Rule in its current form, mortgage brokers will be driven out of business. As a result, consumers will experience a reduction in the availability and access to credit. We ask this Subcommittee and the Financial Services Committee to request that HUD review and revise the Proposed Rule so that it accomplishes HUD's stated goals and objectives to simplify the mortgage process and increase homeownership while not creating competitive disadvantages in the marketplace.

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[34] "Supporting Statement," p. 7.
[35] Executive Order 13272, August 13, 2002.
[36] "Economic Analysis," p. 26.
[37] *See* Attachment 1.

NAMB
National Association of Mortgage Brokers

<u>Attachment 1</u>

Discrepancies in HUD's Economic Analysis and Initial Regulatory Flexibility Analysis[1]

1. On page 22 HUD states that currently, $7.5 billion of YSP payments "is not passed through to borrowers." Under this proposal, HUD assumes that consumers will recapture half of that, or $3.75 billion. The mandate requires a dollar for dollar offset, meaning that consumers should get all $7.5 billion. Where does the other $3.75 billion go?

2. On page 22, HUD states that origination fees are estimated at $15 billion. HUD asserts that the mandate will improve a consumer's ability to shop and therefore capture five percent ($.75 billion). Why wouldn't a broker try to charge more in origination fees if HUD takes away the ability to charge a yield spread premium? In other words, the analysis is static. A small businessman is not just going to voluntarily cut his rates by half – which is what the HUD model assumes. Most small businesses do not have a 50 percent profit margin.

By not producing a more accurate and dynamic model, HUD is overstating the benefits of this proposal and understating the devastating impact on small business who provides high quality service and expertise.

3. The Proposed Rule will allegedly improve a customer's ability to shop and actually facilitate shopping. If this proposal achieves that goal – and it remains unclear at this time – then a customer could go to ABC bank get the GFE and then get in his/her car and drive to Broker X and compare GFE's.

While the ability to shop may be a desired outcome of public policy, it is difficult to accept the notion that increased shopping saves consumers $826 million. The physical act of shopping is not a costless exercise – and, more to the point of HUD's estimate, it does not *save* money. That is, no one pays a consumer for shopping. However, HUD's Economic Analysis ignores this transaction cost and arbitrarily asserts a savings.[2] This overstates the benefits of this proposal.

This is another example of how the static and questionable analysis is fundamentally flawed. As a result, HUD's Economic Analysis provides no basis to understand the real burden of the proposal.

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[1] "Economic Analysis and Initial Regulatory Flexibility Analysis for RESPA Proposed Rule to Simplify and Improve the Process of Obtaining Mortgages to Reduce Settlement Costs to Consumers," U.S. Department of Housing and Urban Development, Office of Policy Development and Research, July 2002.
[2] "Economic Analysis," p. 54.

4. On page 54, HUD states that originators and third party settlement service providers will save time (and $850 million) by reducing the amount of time spent with a borrower. While this may be partially true, HUD does not account for the increased foot traffic and comparison shopping made possible by the new rule. An originator will spend more time answering people's questions that are "shopping." It is quite likely that originators will even be walking these shoppers through the new disclosures. This time and resources is not accounted for in HUD's analysis.

Again, HUD overstates the benefits with static analysis.

5. The last example is how HUD does not understand the marketplace and ends up creating an unlevel playing field for small business.

On page 30 HUD asserts that, "All broker income must be derived from direct fees while lenders who originate may continue to supplement their direct fees with yield spread premiums that continue to be unreported to borrowers. This may give lenders a competitive advantage over brokers." HUD goes on to say on page 32 that "A potential problem comes where a shopper is not knowledgeable. A lender trying to convince a borrower to take his loan instead of the broker's might focus the borrower's attention on the reported origination fee of the two charges…".

That is the point. Of course the lender is going to try to, as HUD says, "convince the borrower to take his loan." That is how the market works. The lender is not an unbiased party in this transaction. He is a competitor and will always try to convince the borrower to take his loan. This is why the current disclosure does not work in its current form – it creates an unlevel playing field.

Attachment 2

National Association of Mortgage Brokers

October 28, 2002

Rules Docket Clerk
Office of the General Counsel
Room 10276
Department of Housing and Urban Development
451 Seventh Street, SW
Washington, D.C. 20410-0500

Re: Docket No. FR-4727-P-01: Real Estate Settlement Procedures Act (RESPA); Simplifying and Improving the Process of Obtaining Mortgages to Reduce Settlement Costs to Consumers

Dear Ladies and Gentlemen:

The National Association of Mortgage Brokers (NAMB) appreciates the opportunity to comment on the referenced proposal (the Proposed Rule), which the U.S. Department of Housing and Urban Development (HUD) published on July 29, 2002. This comment letter begins with a summary of NAMB's position, some background information and general remarks and follows with specific comments on the Proposed Rule.

I. Summary of Position

NAMB has a long history of supporting the reform of the mortgage laws in our country. The laws are complex for both industry and consumers. As such, NAMB provides a proposal to strengthen, simplify and clarify the disclosures of costs provided to consumers in advance of settlement. NAMB believes that its proposal will satisfy the goals set by Secretary Martinez for RESPA reform. NAMB does not support the Proposed Rule's characterization of yield spread premiums as a "lender payment to the borrower" as it will limit consumer choice, render mortgage brokers unable to compete with lenders, and fails to meet the definition as contained in Statement of Policy 1999-1 and clarified in Statement of Policy 2001-1.

However, as a small business, NAMB cannot support the concept of packaging of settlement costs as defined in a regulatory setting. NAMB believes that packaging will lead to monopolies amongst the larger lenders, as small mortgage brokers, and other small settlement service providers, will no longer be able to compete for consumers. The very volatility of the marketplace, especially in recent times, renders many of HUD's proposals in the Proposed Rule untenable at best.[1]

[1] For example, this week alone, interest rates have increased 50 basis points.

II. Background and General Remarks

NAMB is the nation's largest organization exclusively representing the interest of the mortgage brokerage industry. NAMB has more than 13,000 members and 46 state affiliates nationwide. NAMB provides education, certification, industry representation, and publications for the mortgage broker industry. NAMB members subscribe to a strict code of ethics and a set of best business practices that promote integrity, confidentiality, and above all, the highest levels of professional service to the consumer.

Today, the nation enjoys an all-time record rate of homeownership. While many factors have contributed to this record of success, one of the principal factors has been the rise of wholesale lending through mortgage brokers. Mortgage brokers have brought consumers more choices in loan programs and products than they can obtain from a branch office of even the largest national retail lender. Brokers also offer consumers superior expertise and assistance in getting through the tedious and complicated loan process, often finding loans for borrower that may have been turned down by other lenders. Meanwhile, mortgage brokers offer lenders a far less expensive alternative for nationwide product distribution without huge investments in "brick and mortar."

In light of these realities, it is no surprise that consumers have increasingly turned to mortgage brokers. Today, mortgage brokers originate more than sixty percent of all residential mortgages. The rise of the mortgage broker has been accompanied by a decline in mortgage interest rates and closing costs, an increase in the homeownership rate, and an explosion in the number of mortgage products available to consumers. These positive developments are not mere coincidences. They would not have been possible without the advent of wholesale lending through mortgage brokers. NAMB and its members are proud of the foregoing record of accomplishment and our contribution toward consumers' greater access to mortgage finance and homeownership opportunity.

Further, NAMB has engaged in initiatives geared toward increasing the integrity and professionalism of its industry. It has drafted and promoted a model licensing statute for all mortgage brokers across the country. While 46 states and the District of Columbia maintain licensing, registration or notification requirements, NAMB seeks to standardize these requirements. NAMB supports requiring that a loan officer meet certain education requirements, including continuing education requirements. It supports background checks of loan originators to ensure that the bad actors will be forced out of the industry. While initiatives such as the one proposed by NAMB will not eliminate abuses from the mortgage industry, requiring licensing, accompanied by certain screening requirements and education requirements, as described above, will assist in decreasing abuses.

NAMB also believes that the interests of the public and private sector are best served through the voluntary observance of ethical standards of practice, and require that each member subscribe to the following Code of Ethics:

- Honesty and Integrity: NAMB members shall conduct business in a manner reflecting honesty, honor and integrity.
- Professional Conduct: NAMB members shall conduct their business activities in a professional manner.
- Honesty in Advertising: NAMB members shall endeavor to be accurate in all advertisements and solicitations.

- Confidentiality: NAMB members shall avoid unauthorized disclosure of confidential information.
- Compliance with the Law: NAMB members shall conduct their business in compliance with all applicable laws and regulations.
- Disclosure of Financial Interests: NAMB members shall disclose any equity or financial interest they may have in the collateral being offered to secure a loan.

We welcome the opportunity to improve our industry through the reform of mortgage lending laws as well as simplify the process for both consumers and industry.

III. HUD's Proposed Rule on RESPA Reform

NAMB has long supported the reform of the Real Estate Settlement Procedures Act (RESPA), and other federal mortgage lending laws. Together these laws in a valiant attempt to provide consumers with sufficient information about settlement costs and the costs and terms of credit, create more confusion and provide less clarity. NAMB, together with other industry trade groups, has led the way for mortgage reform as well as better, simpler disclosure to consumers. For several years, NAMB met with industry representatives, consumer advocates, members of government-sponsored entities, and HUD to reform RESPA. Unfortunately this process ended with no clear solution, which bespeaks of the complexity of mortgage reform.

As a result of this long history, NAMB continues its support of mortgage reform by supporting Secretary Martinez's desire to simplify the mortgage settlement process for consumers. NAMB also supports the guiding principles HUD has looked to in reforming Regulation X:[2]

- Borrowers should receive settlement cost information early enough in the process to allow them to shop for the mortgage product and settlement services that best meet their needs.
- Disclosures should be as firm as possible to avoid surprise costs at settlement.
- Regulatory amendments should be utilized to remove unintended barriers to marketing new products, competition, and technological innovations that could lower settlement costs.
- Many of the current system's problems derive from the complexity of the process; with simplification of disclosures and better borrower education, the loan origination process can be improved.
- RESPA should be vigorously enforced to protect borrowers and ensure that honest industry providers have a level, competitive playing field.

First and foremost, NAMB strives for a level playing field for all mortgage originators. It is the basic tenet of NAMB's policy towards mortgage reform. However, mortgage brokers should not be singled out and HUD's Proposed Rule does just that – indirect compensation **for mortgage brokers only** must be disclosed as a lender payment to the borrower, mortgage brokers must obtain the signature of a lender when packaging settlement services, and others. We are disappointed that HUD acknowledges that the proposed rule "results in different treatment of compensation in loans originated by lenders and those originated by mortgage brokers."[3] NAMB strives to level this playing field, equaling the opportunity for both mortgage brokers and mortgage lenders.

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[2] Real Estate Settlement Procedures Act, 67 Fed. Reg., 4,135 (July 29, 2002).
[3] Proposed Rule, Fed. Reg. at 49,148.

IV. Increased Consumer Education and Enforcement is Paramount to Ending Abusive Practices

A. Increased Consumer Education will Create a Consumer Base More Cognizant of Abusive Lending Practices

NAMB remains convinced that consumer education is paramount in forestalling abusive lending practices. As certain television commercials stated years ago, "an educated consumer is our best customer." Greater regulation may lead to more confusion amongst consumers; the focus is better spent on consumer education.

Increased consumer education will provide a consumer base that can recognize abusive practices in the mortgage industry. NAMB has long established success in providing professional development education to our industry. As a recognized leader in grassroots education, we created a consumer education program, specifically geared to potential first-time minority homebuyers. Our program, *Are You Prepared to Head Down the Road to Home Ownership?*, is a grassroots level initiative that allows industry professionals to conduct informative presentations in local offices, churches, community centers, and other neighborhood venues. The presentation provides elementary level information on the pros and cons of homeownership, what to consider before purchasing a home, and basic information on the home-buying process.

This program will be introduced at NAMB's 1st Annual National Housing Fair in Washington, DC in March of 2003 to give the first-time homebuyer the opportunity to address the fears, hopes and concerns of homeownership. The event will include mortgage professionals and experts who can discuss the availability of affordable housing programs, strategies for obtaining a down payment as well as responsible credit repair. NAMB believes this will complement the homebuyer seminar kits its members already use to promote neighborhood housing seminars for emerging markets and first-time homebuyers.

NAMB looks forward to working with HUD to expand consumer education and hopes that HUD will make consumer education a priority in the years to come.

B. Additional Regulation is Meaningless Without Stronger Enforcement

Also, revision of Regulation X will be virtually meaningless if enforcement is not increased to a level which dramatically impacts the "bad actors" in our industry. NAMB has long been a proponent of the expulsion of members of our industry who defraud consumers. However, we have also long been proponents of the maxim that increased regulation bears no impact without increased enforcement. Bad actors will remain in the industry, flying low below the radar screens of HUD and other regulators, without increased enforcement.

Recently HUD has taken steps to increase enforcement of laws and regulations and we commend HUD for this first step. However, the past inactivity has left its hallmark in that there are members of the mortgage industry who flaunt the law. HUD should look at new an innovative methods for ensuring that these actors never enter the industry again. For example, we suggest that HUD publicize enforcement actions in local and national newspapers to alert the public of these individuals or companies. Increased awareness will assist in enforcement efforts. We urge HUD to take dramatic steps in increasing the enforcement of current laws and regulations before implementing new laws or regulations.

V. The Proposed Rule Should Not Provide Additional Barriers for Minority Homeownership

President Bush and Secretary Martinez have been very vocal in their goal of increasing minority homeownership. Minority homeownership has recently been on the rise; in a press release dated April 24, 2002, the U.S. Census Bureau released data that showed that homeownership among Hispanics rose substantially to 46 percent.[4] However, as noted in other press releases, a Bush Administration analysis showed that "a large gap still exists between minority and white households."[5] The analysis showed that "since 1994, when the black homeownership rate was 27.5 percentage points below the rate of whites and the Hispanic rate was 28.8 percentage points below, only small gains have been made."[6] The analysis further showed that "by 2001 the gap had been reduced by just 1.6 percentage points for African Americans and 1.8 percentage points for Hispanic households."[7]

HUD's analysis identified several barriers for homeownership: "(i) lack of capital for the down payment and closing costs, often the single greatest barrier to homeownership; (ii) lack of access to credit and poor credit histories, which means more minority families are rejected for a mortgage loan or given loans with high interest rates; (iii) lack of understanding and information about the homebuying process, especially for families for whom English is a second language;" and (iv) others.[8]

Mortgage brokers are the key to bridging the gap in minority homeownership. Mortgage brokers are integral members of their community and provide access to credit, especially in rural areas, that most large lenders cannot. Further, mortgage brokers are willing to take the time to work with minority consumers, who often have non-traditional sources of income, and other issues. A recent study performed by Wholesale Access, a research, advisory and publishing company, on minority lending stated that two of the key findings of this research are: "(i) brokers reach more minorities than lenders; and (ii) the explanation for this is found in their locations, products and staffing."[9] Many of these communities would not have the availability of mortgage loans currently enjoyed today were it not for mortgage brokers, who originate more than 60% of all mortgage loans today.[10] Mortgage brokers often originate loans for "difficult borrowers," those who are credit challenged, have income that is difficult to document, or are first time homebuyers. Mortgage brokers spend the time with these applicants, working together with them, to work through credit problems, having no credit histories, and other issues to help these individuals finance the purchase of their home. Any rule implemented by HUD should not disproportionately adversely impact mortgage brokers. NAMB believes that its proposal levels the playing field for all loan originators while being beneficial to consumers.

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[4] Press Release, Department of Housing and Urban Development, Homeownership Increase Among Hispanics (April 24, 2002) (on www.hud.gov).
[5] News Release, Department of Housing and Urban Development, New HUD Report Identifies Barriers to Minority Homeownership, Outlines Bush Administration Actions to Overcome them (June 17, 2002) (on www.hud.gov).
[6] *Id.*
[7] *Id.*
[8] *Id.*
[9] Press Release, Wholesale Access, Study of Minority Lending Completed, (Sept. 24, 2002) (on www.wholesaleaccess.com).
[10] Prepared Statement of Mr. David Olson, President, Olson Research, U.S. Senate Committee on Banking, Housing, and Urban Affairs Hearing on "Predatory Lending Practices: Abusive Uses of YSPs," January 8, 2002.

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VI. NAMB's Concerns with HUD's Proposed Rule in Connection with the Enhanced Good Faith Estimate

A. Characterization of Yield Spread Premiums as a Lender Payment to the Borrower

Characterizing yield spread premiums as a lender payment to the borrower creates *unintended consequences* and *provides less clarity* to consumers than as presently disclosed. In the Proposed Rule, HUD seeks meaningful disclosure of mortgage broker fees to borrowers. However, the proposed method of disclosure achieves just the opposite – it muddies the waters as to how indirect broker compensation works in reality. Under the proposed structure, indirect broker compensation is disclosed as a "lender payment to the borrower for higher interest rate."[11] Not only is this inflammatory, it seems to discount HUD's own Statement of Policy, in which it states that yield spread premiums can be payments for goods, services, and facilities provided to the lender by the mortgage broker. NAMB believes that HUD's characterization of yield spread premiums creates a multitude of problems, not the least of which is a new round of class action lawsuits.

It seems obvious that a consumer's initial reaction to this characterization will be one question – "where is my check?" As stated elsewhere in this comment letter, a cottage industry has sprung out of Section 8 litigation – class action lawsuits. In recent years, yield spread premiums have been under fire, as well as mark-ups of third party settlement service fees. Such a departure from HUD's established (in Statement of Policy 1999-1) and reemphasized (in Statement of Policy 2001-1) "definition"[12] of yield spread premiums will only spur another round of litigation. Further, a borrower claiming fraud, when no check appears, will seek counsel to litigate the issue. Unfortunately, the stark reality of business is that any increase in the amounts of money spent in defending any lawsuits will ultimately be passed through to the consumer in the form of higher costs for originating a mortgage loan. NAMB fears this very real and distinct threat of liability as well as the potential costs of defending the legitimate use of this method of compensation.

Such a characterization constitutes a reversal of HUD's definition of a yield spread premium in Statements of Policy 1999-1 and 2001-1. Yield spread premiums, and other indirect compensation, have historically not been viewed merely as payment for goods or facilities provided and services performed to the borrower. HUD states in the background on the proposed rule that "as retailers, brokers also provide the borrower **and the lender** [emphasis added] with goods and facilities such as reports, equipment, and office space to carry out retail functions."[13] In utilizing mortgage brokers, wholesale lenders can provide mortgage loan products at conceivably lower rates and lower costs to consumers. Thus, characterizing

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[11] Proposed Rule, Fed. Reg. at 49,164.

[12] In Statement of Policy 1999-1, HUD stated that yield spread premiums were not *per se* illegal. The Statement of Policy states that "in determining whether a payment from a lender to a mortgage broker is permissible under section 8 of RESPA, the first question is whether goods or facilities were actually furnished or services were actually performed for the compensation paid." Real Estate Settlement Procedures Act, 64 Fed. Reg. 10,080, 10,084 (March 1, 1999). "The second question is whether the payments are reasonably related to the value of the goods or facilities that were actually furnished or services that were actually performed." *Id.*.

[13] Real Estate Settlement Procedures Act, Fed. Reg. at 49,140. HUD details in the proposed rule that "mortgage broker essentially 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." *Id.*

yield spread premiums as lender payments to the borrower is inaccurate as the lender may compensate the mortgage broker for providing brick and mortar, and other goods and facilities.

Also, in singling out indirect compensation to mortgage brokers only, HUD goes against its own statements in Statement of Policy 2001-1. In this Policy Statement, HUD states that it is "aware that while yield-spread premiums are not used in loans originated by lenders, lenders are able to offer loans with low or no up-front costs required at closing by charging higher interest rates and recouping the costs by selling the loans into the secondary market for a price representing the difference between the interest rate on the loan and the par, or market, interest rate. Sale of such a loan achieves the same purpose as the yield spread premium does on a loan originated by a broker. **The department strongly believes that all lenders and brokers should provide the level of consumer disclosure that the purposes of RESPA intend and that fair business practices demand [emphasis added].**"[14] Disclosure that lenders also receive indirect compensation on the sale of the loan on the secondary market should also be required.

Additional conflicts arise in connection with the following: (i) brokers will cease originating FHA and VA-insured mortgage loans due to origination fee caps; (ii) contracts between mortgage brokers and wholesale lenders in connection with "flipping" will be void, causing the only recourse to be demanding the lender payment to the borrower back from the borrower; (iii) mortgage lenders having to provide consumers with a 1099 form for income from the lender; (iv) potential tax consequences; (v) causing more loans, including some conventional loans to be subject to state predatory lending laws; (vi) causing mortgage brokers to cease advertising "no point loans" while allowing its competitors to continue to do so; and (vii) others. These points are further elaborated on in NAMB's response to Question 7 as contained in the Proposed Rule.

B. NAMB's Proposal for Reform of RESPA's Disclosure Requirements

NAMB wants to work with HUD in strengthening the good faith estimate to end abusive practices with the disclosure of settlement costs. Legislative change will ensure that there are no challenges in the courts over whether HUD has the authority to effect these changes. By strengthening the disclosure requirements to the consumer, NAMB believes that many of the abuses facing consumers will cease to exist as unscrupulous originators will no longer be able to effect a "bait and switch" to more expensive loan products. Further, we support the addition of penalties and remedies for consumers when the requirements for NAMB's proposed disclosure are not met. Finally, NAMB believes that standardization of the disclosure process and forms will benefit both consumers and industry. Detailed below is NAMB's proposal for providing for a stricter good faith estimate of settlement costs. Further, NAMB's proposed disclosure is attached to this letter as Exhibit A, and we ask that Exhibit A be included for the record.

i. Disclosure Requirements

a. Origination Costs, Settlement Costs, Interest Rate, Monthly Payment

Under NAMB's proposal, the costs to originate a mortgage loan will fall into two categories: (i) origination costs, which are paid by the consumer directly to the lender and/or the mortgage broker; and (ii) settlement costs, which are all fees paid to a third party for services rendered in originating a mortgage loan (with the exception of mortgage insurance, hazard insurance, real property taxes, escrows for the

[14] Real Estate Settlement Procedures Act, Statement of Policy 2001-1, 66 Fed. Reg. 53,052, 53,057 (October 18, 2001).

previous items, and per diem interest). These fees will be disclosed to consumers on the front page of a new form (also proposed by NAMB) in simple highlighted boxes, together with a description of what constitutes these fees.

In connection with origination costs, these fees are guaranteed unless certain events occur. These events include: (i) when a consumer is not eligible for the loan program; (ii) when the property proposed to secure the loan changes or does not qualify; (iii) the consumer chooses a different loan program, (iv) the consumer chooses a different pricing option; and (v) when the loan amount changes. These events must be documentable, maintained in the loan file, and the originator must comply with the Equal Credit Opportunity Act[15] (ECOA) and the notice requirements more fully regulated under Regulation B,[16] the implementing regulation for ECOA.

In connection with settlement costs, these costs are estimated within three (3) business days of "application," as defined under Regulation X. Once the consumer accepts the disclosure, an originator proceeds with the origination of the loan, and collects and documents the proper data for the mortgage loan. If there are any changes in the settlement costs, at a minimum of fifteen (15) days prior to closing, the originator must provide a redisclosure to the consumer (if there are no changes, an originator is not required to redisclose). At this time, the settlement charges cannot increase between redisclosure and settlement more than 10% of the total costs at settlement. NAMB believes that this provides the originator with adequate time to underwrite the loan and utilize the third party services. Further, the consumer will be notified of firmer third party costs fifteen (15) days prior to settlement. At this time, a consumer will be required to either reject the disclosure or accept the disclosure by authorizing the drawing of loan documents.

Redisclosure is also required when a consumer chooses to lock their interest rate, when the consumer does not lock their interest rate upon initial disclosure. However, the tolerance does not apply in this instance. The same fifteen (15) day rule, as described above, applies in these instances.

NAMB believes that the redisclosure requirements will be more effective in combating bait and switch than is currently required under RESPA. A consumer will have time to turn down the loan (if the loan charges do not meet their understanding), and still seek another mortgage loan. Bait and switch will never cease to exist; unscrupulous actors will always be able to engage in this practice. NAMB does offer one potential solution; we recommend that HUD work with the Federal Reserve Board in strengthening the details required to be provided in the adverse action notices and counteroffer notices.

The form will also disclose the interest rate of the mortgage loan. This rate will be subject to change, unless the consumer locks the interest rate. The form provides an opportunity for the consumer to lock the interest rate, and provides a place where the consumer may execute the agreement to lock. The amount of the lock-in fee is to be disclosed in this box. The consumer is also provided a warning that if the consumer does not choose to lock their interest rate, the interest rate may change without any notification. Consumers will be asked to acknowledge, regardless of whether the consumer locks or floats their interest rate.

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[15] 15 U.S.C. § 1691 *et seq.*
[16] 12 C.F.R. § 202 *et seq.*

The form also discloses the amount of the monthly payment for the consumer. This box contains an opportunity to acknowledge whether the monthly payment includes principal (for interest only balloon payment loans), interest, escrows for real property taxes, hazard insurance, and mortgage insurance. This information is very helpful to consumers in that some consumers are not aware whether they must arrange for payment of these items outside of their monthly payment. Consumers will not be surprised by this information.

Finally, itemization of the fees included in origination costs and settlement costs are disclosed at the bottom of the first page of the form. We understand that HUD believes that the less numbers on the form the better for shopping, but mortgage brokers know that consumers will ask what fees constitute these two categories. NAMB supports the continued itemization of fees (please note that the fees included at the bottom of the form are representative of those charged, additional fees may be necessary that are not itemized on NAMB's proposed form). Further, consumers will be able to compare this information to the HUD-1 with much greater ease and clarity than under the Proposed Rule. However, NAMB believes that the HUD-1 should be revised to be consistent with any amendments to the good faith estimate requirement. Thus, under NAMB's proposal, the fees on the HUD-1 should be redistributed to fall into the category of origination costs, settlement costs, or other estimated costs.

b. Other Information Disclosed

The form will also discuss the services that the originator might perform in connection with the origination of the mortgage loan, as well as provide a warning to consumers to utilize the good faith estimate form at settlement for comparison purposes. The form also warns consumers that the originator does not guarantee the lowest price or the best terms available in the market.

The proposed form also provides the following information: (i) loan amount; (ii) term of the loan; (iii) assumability of the mortgage loan; (iv) property address; (v) whether the loan is for a purchase or refinance; (vi) whether the loan is a first mortgage loan or a subordinate mortgage loan; (vii) loan program; (viii) whether the loan has a prepayment penalty, and if so, the terms of the prepayment penalty; (ix) whether the loan has a balloon payment, and if so, the terms and amount of the balloon payment; (x) whether the loan is an adjustable rate mortgage loan; and (xi) an estimation of the amounts for hazard insurance, property taxes, mortgage insurance, escrow amounts, and per diem interest.

The proposed form will also disclose the maximum amount of yield spread premium that will be paid to the mortgage broker. The yield spread premium will be characterized as compensation for goods, facilities and services. Further, the proposed form will contain the following language: "An originator may be compensated by an investor for goods, facilities or services provided to you or to the investor. This will result in a higher interest rate for this loan. If you would rather pay less cash up front, you may be able to pay some or all of the originator's compensation indirectly through a higher interest rate. If you would rather have a lower interest rate, you may pay higher up-front points and fees. This amount will not exceed the amount disclosed to the left of this description. If the originator is acting as a lender in this transaction, the originator may receive additional compensation when it sells the loan for the value of the servicing rights or the value of the interest rate or a combination of both. This amount is not required to be disclosed." NAMB believes that this disclosure is more in keeping with HUD's earlier Statements of Policy (as discussed in NAMB's response to Question 7 in this letter), Further, we believe that this will eliminate many of the problems that exist with the Proposed Rule's characterization (also discussed in NAMB's response to Question 7 in this letter).

Above this disclosure, NAMB's form includes the Proposed Rule's information on "Interest Rate and Settlement Costs Options." Together with this description, the form includes a generic chart showing an example of how an increase or decrease in interest rate can affect a person's monthly payment. Currently, the HUD proposed rule requires originators to create a "sample" chart, on a loan-by-loan basis, that would provide the consumer with comparisons of the options available for payment of settlement costs to lower the consumer's interest rate. However, the volatility of the marketplace renders this requirement virtually untenable. An originator will have difficulty in complying with this requirement as the market changes too rapidly for a loan originator in the field to create in the manner contemplated in the proposed rule. NAMB, however, sees the utility for consumers to have this type of information for comparison and for the purposes of "shopping." As such, we find a workable middle ground to be the inclusion of a generic "sample" chart.

Finally, the form provides "Details of Transaction" together with a requirement that an estimation of the amount to be paid at closing be disclosed. NAMB recommends that this information be provided as a summary of the details of the transaction, which parallels the form on the Uniform Residential Loan Application Form 1003.

c. Execution Requirements

This disclosure is required to be signed by the consumer, initially and at redisclosure, and returned to the originator and maintained in the file. Further, at redisclosure, the consumer authorizes the drawing of closing documents. Consumers are provided a seven (7) day period in which to return the executed disclosure. This will prevent unscrupulous originators from merely marking the disclosure as "sent" and placing the bogus form in the file. NAMB believes that this is a flaw in the current RESPA structure.

ii. Length of Time Fees are Guaranteed Until Acceptance

In order to facilitate shopping, NAMB's proposal provides that the guaranteed origination costs will remain available to a consumer for seven (7) days from initial disclosure. At this point, the consumer either accepts the disclosure or rejects the disclosure. Once the consumer accepts the disclosure, the origination fees are guaranteed (unless certain conditions are met and documented, as described above). A consumer also at this point can elect to lock their interest rate or float their interest rate. Once a consumer accepts the disclosure, an originator can proceed with underwriting the loan. It is at this point that a consumer could be required to pay additional costs (if allowable under state law). The same seven (7) day period applies in connection with redisclosure. However, this seven (7) day period does not detract from the fifteen (15) day period; that is, if the originator rediscloses fifteen (15) days prior to settlement, and the consumer takes the full seven (7) days to return the authorization, the closing may take place in eight (8) days.

iii. Redisclosure Requirements

An originator will be required to redisclose in several instances. First, an originator must redisclose at a minimum of fifteen (15) days prior to settlement if any of settlement costs initially disclosed have increased. This is addressed above. An originator will also be required to redisclose, within three (3) business days of notification of a counteroffer, upon certain conditions, which are documentable: (i) when a consumer is not eligible for the loan program; (ii) when the property proposed to secure the loan changes or does not qualify; (iii) the consumer chooses a different loan program, (iv) the consumer chooses a different pricing option; and (v) when the loan amount changes. As discussed above, NAMB believes that the redisclosure requirements will be effective in stopping bait and switch practices, as well as provide the originator an effective tool to combat borrower fraud. As stated later in this letter, borrower fraud is much more prevalent in this industry than assumed.

A consumer may waive the redisclosure period (i.e., the fifteen (15) day period). This can only be done if the borrower signs a waiver to this effect. While NAMB believes this can be open to abuse, many consumers, especially in a refinancing, will not want to wait fifteen (15) days to close. A consumer should be made to hand-write the reasons for the waiver and this request must be maintained in the loan file. Further, an originator is not required to redisclose if the costs disclosed initially have not increased. Thus, the fifteen (15) day period would not be applicable in this instance.

iv. Remedies and Penalties

Finally, in order to truly strengthen the disclosure of costs, NAMB's proposes that HUD include additional remedies and penalties that are available to the consumer, a limited right to cure that is available to industry, and draconian penalties that would be imposed if the originator does not exercise the right to cure. Part of the reason for the bait switch tactics that many contend are occurring today is the failure of RESPA to contain any remedies that will impact the bad actors. However, that said, good actors in the industry must be given an opportunity to cure any overpayments before penalties are waged against them.

The Proposed Rule allows that if the cost at settlement exceeds that which was disclosed on the enhanced good faith estimate, all loan-related fees can be refunded if the borrower withdraws the application.[17] This places industry at a disadvantage as certain third party fees (i.e., the credit report and appraisal) may have already been paid for services rendered. Remedies should also be available to industry. An originator should have the right to cure the overpayment. If the originator refuses to cure the overpayment, a consumer should then be able to withdraw the application and receive a refund of all loan-related fees and charges as described in the proposed rule. To allow the proposed remedy at the outset without providing a right to cure places a burden on the originator. A right to cure should be permitted under this rule.

C. NAMB Expresses Concern that HUD is Acting the Beyond Scope of its Authority Which Will Result in Legal Challenges

HUD's Proposed Rule, if implemented, would create the most extensive and far reaching changes to the mortgage settlement process since the implementation of the 1975 amendments to RESPA. Originally, RESPA required "at the time of loan commitment, but in no case later than twelve calendar days prior to settlement, ...an itemized disclosure in writing of each charge arising in connection with such settlement."[18] Further, the statute provided that "in the event the exact amount of any such charge is not

[17] The language is as follows: "If the cost at settlement exceeds the estimate reported on the good faith estimate, absent unforeseeable and extraordinary circumstances, the borrower may withdraw the application and receive a full refund of all loan-related fees and charges." Proposed Rule, Fed. Reg. at 49,159.
[18] Real Estate Settlement Procedures Act of 1974, Pub. L. No. 93-533, § 6(a), 88 Stat. 1724, 1726 (1974).

available, a good faith estimate of such charge may be provided."[19] The statute provided for certain remedies for failure to provide the disclosure to the consumer.[20]

In 1975, Congress passed amendments to RESPA repealing the above disclosure provisions and replacing them with the language that we are familiar with today.[21] In this language Congress requires that "a **good faith estimate of the amount or range of charges** for specific settlement services that the borrower is **likely** to incur in connection with the settlement" of the mortgage loan [emphasis added] be disclosed to consumers "as prescribed by the Secretary."[22] Further, these amendments eliminated the penalties contained in the 1974 statute.[23]

The reasoning for these changes were captured in the legislative history for the 1975 amendments which stated that "the major purpose of this provision of RESPA is to afford the buyer and the seller the opportunity and the time to shop for settlement services at prices lower than those charged for services arranged by the lender."[24] It further stated that "another purpose of this provision is to protect the buyer and the seller against unexpected or unreasonable charges which might be imposed at the time of settlement."[25] Yet, in endorsing the elimination of the early disclosure, the history relays the belief that "while advance disclosure provisions of RESPA are a logical way to reach toward these objectives they are neither necessary nor, as experience has borne out, desirable."[26]

It is uncertain as to whether HUD has the authority to make such sweeping changes to the good faith estimate requirements under RESPA. It appears that any changes to the good faith estimate requirements in order to strengthen the disclosure requirements would be ripe for judicial challenge without corresponding legislative authority.[27]

This position seems bolstered further by Congress's use of "good faith" in the statute. Even if one were to take an expansive view on what constitutes "good faith," it does not seem arguable that statutory authority expands to a guarantee or even disclosing within a prescribed tolerance of settlement costs. As HUD itself cites in the Proposed Rule, "Differing editions of Black's Law Dictionary have defined 'good faith' as 'a state of mind consisting in * * * honesty in belief or purpose * * * [and faithfulness to one's duty or obligation,' and 'freedom from knowledge of circumstances which ought to put the holder upon inquiry' as well as 'absence of all information, notice, or benefit or belief of facts which render [a transaction unconscientious.' Inherent in these definitions is the concept that where a party makes an estimate in good faith they will take into account all relevant information available to them, and will exercise reasonable

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[19] *Id.*

[20] RESPA provided that, if a lender failed to provide a consumer with the required disclosure, the lender would be liable for "the actual damages involved or $500, whichever is greater, and in the case of any successful action to enforce the foregoing liability, the court costs of the action together with a reasonable attorney's fee as determined by the court." Real Estate Settlement Procedures Act of 1974, Pub. L. No. 93-533, § 6(b), 88 Stat. 1724, 1726 (1974).

[21] This language is as follows: "Each lender shall include with the booklet a good faith estimate of the amount or range of charges for specific settlement service the borrower is likely to incur in connection with the settlement as prescribed by the Secretary." 12 U.S.C. § 2604(c).

[22] *Id.*

[23] *Id.*

[24] H.R. Rep. No. 94-667, at 4 (1975), *reprinted in* 1975 U.S.C.C.A.N. 2448, 2451.

[25] *Id.*

[26] *Id.*

[27] This was cited to in the "Joint Report to the Congress Concerning Reform to the Truth and Lending Act [sic] and the Real Estate Settlement Procedures Act," prepared by HUD and the Federal Reserve Board in July 1998.

care in ascertaining and evaluating such information before providing such an estimate."[28] Mortgage brokers and other originators comply by this requirement today. These originators use the information gathered from the consumer, such as value of the home, the loan amount, a consumer's credit history, income and other information, to provide a consumer with an estimate in good faith of the settlement costs.

While NAMB looks forward to working with HUD to strengthen the good faith estimate of settlement costs, it seems that in order to avoid any potential challenge in the courts based upon the legislative history, and the language of the statute itself, legislative authority must be sought. NAMB hopes that it can work with HUD in promoting this proposal to Congress as a balanced proposal that benefits both industry and consumers.

V. NAMB's Concerns with HUD's Proposed Rule with the Packaging of Settlement Services

NAMB believes that mortgage brokers, as small businesses, will be greatly disadvantaged by the "regulatory driven packaging" (as opposed to market driven packaging) of settlement services.[29] Mortgage brokers, as small businesses,[30] do not have the bargaining power to enter into volume-based discounts with third party settlement service providers as do larger entities. Under the Proposed Rule, mortgage brokers would not be able to compete with the larger entities and will be forced to cease the transaction of business, become an agent for one lender or two, utilizing their packages or utilize the good faith estimate approach, which could also disadvantage mortgage brokers. This will force mortgage brokers to lose their autonomy, which is beneficial to consumers in the form of more consumer choice.[31] This impact will be passed through to the consumers in the form of higher costs and less consumer choice. As such, NAMB cannot support the "regulatory driven" concept of packaging.

Further, the packaging of settlement services is occurring today.[32] Thus, the removal of regulatory barriers is not necessary to allow packaging of settlement services;[33] rather, exemption from Section 8 liability creates an incentive for entities to offer packages. While HUD contends that packaging will decrease a consumer's settlement costs as competition drives these prices down, it could also work to

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[28] Porposed Rule, Fed. Reg. 49,150.

[29] Recent news articles have cited a decline in small business hiring, "creating another headwind for the nation's stubbornly sluggish economy recovery." *Small-business Hiring Dip Slows Recovery,* Ariz. Republic, Oct. 25, 2002, at D-1. Further, an article cites that "small businesses make up 98 percent of all enterprises in the nation and create about 65 percent of jobs." *Id.*

[30] The majority of mortgage brokers are small businesses. The Small Business Association defines "small businesses" for "loan brokers" as being those with $5 million in annual receipts. 13 C.F.R. § 121.201. The Economic Analysis cites to a study in which it stated that most mortgage broker firms consist of one office and five employees (including the owner). "Economic Analysis and Initial Regulatory Flexibility Analysis for RESPA Proposed Rule to Simplify and Improve the Process of Obtaining Mortgages to Reduce Settlement Costs to Consumers," U.S. Department of Housing and Urban Development, Office of Policy Development and Research, July 2002, p.12. Further more, this study stated that it found "brokers as low-cost, highly competitive firms, vigorously competing with one another and with little opportunity to earn above-normal profits." *Id.*

[31] Currently, mortgage brokers work with many different lenders. This provides a consumer with a choice of hundreds of different loan products, much more than those available from a mortgage lender. This is one reason for the rise in the number of originations by mortgage brokers over recent years.

[32] Mortgage.com, a division of ABN AMRO Mortgage Group, Inc., is currently offering a guaranteed package of certain settlement services together with a mortgage loan on its website, www.mortgage.com.

[33] Proposed Rule, Fed. Reg. at 49,136.

drive prices up as packagers can "up charge" costs with no Section 8 repercussions.[34] HUD's longstanding prohibition against the "up charging" of third party settlement costs will cease to exist only for those who package. Those who choose to operate under the enhanced good faith estimate will still be subject to this prohibition.

NAMB also believes that there are many unworkable provisions in HUD's Proposed Rule in connection with packaging. These provisions include, among others, providing a index for consumers to track their interest rate, allowing a consumer thirty (30) days to shop for loan while the package is available, providing no itemization of costs that are in the package, allowing the package to remain viable, after acceptance, indefinitely, together with others. Perhaps one of the most important aspects of the Proposed Rule, which is not addressed, is the need for federal preemption of state laws of the Proposed Rule to have the effect desired. NAMB addresses the need for federal preemption in response to the Proposed Rule's Question 22.

Mandating "regulatory driven packaging" seems to eliminate competition which is one of the reasons mortgage pricing has been kept so low.[35] As mortgage brokers will not be able to participate in the packaging world, they will be driven to utilize the enhanced good faith estimate. The good faith estimate, especially the proposed characterization of yield spread premiums, is fraught with pitfalls which do not allow a mortgage broker to compete with lenders.

Finally, any changes made to the initial disclosures to consumers must be reflected in the HUD-1 Settlement Statement. In not altering the HUD-1 Settlement Statement, the consumer will be faced with the confusing compilation of costs and have a difficult time in comparing the two documents.

A. NAMB Believes that HUD's Proposed Rule's Provisions on Packaging Will Create a Monopolistic Environment to the Detriment of Consumers

HUD claims that the less efficient originators will suffer under the Proposed Rule but the more efficient originators will prosper. A mortgage broker may be the most efficient mortgage broker working today but when placed in competition for costs with a multi-billion dollar originator, the efficient mortgage broker will still be unable to compete and will lose business. Efficiency cannot beat might.

However, as stated above, under HUD's Proposed Rule, many mortgage brokers will not be able to compete. The larger entities will have the advantage of size when entering into volume-based contracts with third party settlement service providers. Thus, the larger entities will be able to cut their prices, provide consumers with packages at a lower price, and force mortgage brokers to provide the enhanced good faith estimate to consumers. Again, this is not a matter of efficiency; rather it is a matter of might. <u>This creates a new unlevel playing field for mortgage brokers as detailed in this letter.</u>[36] But it does not end there.

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[34] Further, HUD's Economic Analysis contains some flawed conclusions as to the true savings to consumers which we detail below.

[35] A study cited to in HUD' "Economic Analysis" stated that it found "brokers as low-cost, highly competitive firms, vigorously competing with one another and with little opportunity to earn above-normal profits." "Economic Analysis," p. 12.

[36] As detailed in this letter, NAMB finds many provisions of the Proposed Rule's enhanced good faith estimate unworkable.

As mortgage brokers will be unable to compete with the larger entities, mortgage brokers will no longer be able to utilize the local title companies, local appraisers, local attorneys, and others for the provision of third party settlement services. The adverse impact HUD's proposed use of packaging will have an exponential impact on many small local companies.

Perhaps who will suffer the most will be the consumers. Additional consolidation will occur in the mortgage lending industry and competition will begin to slow down as the number of "originators" decreases. Lenders might be incented by market share not to pass any discounts to consumers; under HUD's Proposed Rule there would be no repercussions under Section 8 for this failure. History has shown that monopolies do not drive down costs; while in some instances it might, most monopolies drive costs up (which necessitated the passage of the Sherman Anti-Trust Act).

Another by-product of "regulatory driven packaging" is the loss of independence on the part of mortgage brokers, as well as third party service providers. Mortgage brokers, if the packaging world is the only viable alternative as opposed to risking potential lawsuits over the Proposed Rule's characterization of yield spread premiums (if the Proposed Rule is finalized in its present incarnation), will become "agents" of one or two lenders. Mortgage brokers who today can offer consumers hundreds of mortgage products, will only have a dozen or so to offer consumers. Further, settlement service providers will be subject to pressure from lenders to provide information (such as appraisals or title reports) that meet the expectations of that lender. For these reasons, NAMB cannot support the concept of "regulatory driven packaging" (as opposed to packaging driven by the market).

B. NAMB Believes that Certain Misconceptions Exist Over the Role of a Mortgage Broker

As stated above, today, the nation enjoys an all-time record rate of homeownership. While many factors have contributed to this record of success, one of the principal factors has been the rise of wholesale lending through mortgage brokers. Mortgage brokers have brought consumers more choices in loan programs and products than they can obtain from a branch office of even the largest national retail lender. Brokers also offer consumers superior expertise and assistance in getting through the tedious and complicated loan process, often finding loans for borrower that may have been turned down by other lenders. Meanwhile, mortgage brokers offer lenders a far less expensive alternative for nationwide product distribution without huge investments in "brick and mortar."

However, mortgage brokers are not merely conduits for the wholesale mortgage market. Rather, mortgage brokers serve the role as advisor, credit counselor, underwriter, personal contact, and others to the consumer. Consumers who work with large lenders frequently never even see their loan officer. Mortgage brokers often work with a consumer for long periods of time (some even up to a year or more) to obtain their mortgage loan. Mortgage brokers work with consumers through changes in the property to be secured, different economic circumstances, such as loss of a job, income that is difficult to document (such as seasonal), and challenged credit. A mortgage broker does not simply press a few keys to provide the consumer with a mortgage loan. Nor are mortgage loans akin to products that can be lifted from the shelf and paid for at checkout. Mortgage brokers perform a vital and sometimes difficult role in assisting consumers obtain a mortgage loan.

For example, a real life example of certain difficulties in originating a mortgage loan is as follows. A mortgage broker took an application from a customer in November of 2001. The consumer wanted to refinance their mortgage loan in order to renovate their home. After the loan had been approved, the consumer had second thoughts about refinancing as opposed to selling their home. After several months, the consumer decided to sell their house and purchase a new home. The mortgage broker worked with consumer for financing for the future home purchase but the home did not sell. The consumer then decided to continue with the refinancing but ultimately refinanced their home and purchased a second home simultaneously. The mortgage broker in question worked hand in hand with the consumer for ten months in order to help with their financing needs.

C. Today's Economy

The housing market remains one of the few working aspects of our economy. A recent article entitled "House Prices Redux," in www.economy.com, stated that "quickly rising house prices have been crucial to mitigating the impact of falling stock prices on consumers. Housing has once again overtaken stocks as the largest asset in the household balance sheet. Rising house prices and homeowners' equity have also facilitated the unprecedented mortgage refinancing boom, which, in turn, has supported household cashflow as mortgage debt payments have fallen for some refiers [sic] and it has allowed others to raise cash through cash-out refis [sic]."[37] Questions arise as to whether introducing new and complex price capping features and disclosure methods will adversely impact the market slowing down access to credit as well as driving up costs for consumers to compensate for the increased costs in instituting new procedures, software and training for loan officers. Could HUD perhaps be opening a Pandora's box? Based upon HUD's Economic Analysis, it is uncertain at best.

D. HUD's Economic Impact Analysis is Flawed, Inconsistent and Incomplete

HUD's Economic Analysis provides detail on HUD's expectations as to the savings the Proposed Rule, if finalized, will Economic Analysis and Initial Regulatory Flexibility Analysis, NAMB finds that the analysis is flawed and inconsistent in many instances. While we believe that HUD had the best intentions in having this analysis performed, NAMB believes that further analysis is necessary to ensure that the numbers professed in the Analysis bear out the impact any portion of the Proposed Rule will have in the marketplace.

In accordance with the requirements of the Proposed Rule, NAMB submitted a comment letter on the impact the Proposed Rule has on the Paperwork Reduction Act of 1995.[38] In this comment letter, NAMB cited to several inconsistencies between the information in the Economic Analysis and HUD's Paperwork Reduction Act Submissions to the Office of Management and Budget (OMB). We repeat several of those in this comment letter to impress that the presence of these inconsistencies. Also, greater analysis is called for based upon the proposed dramatic impact the Proposed Rule, if finalized, will have on the mortgage industry for both industry and consumers. Finally, the disproportionate impact on small business necessitates further analysis under the Regulatory Flexibility Act.[39]

The Proposed Rule requires additional disclosures for mortgages originated by mortgage brokers. The increased regulatory burden will lead to an increase in the cost of doing business and will initially result in an increased cost to the consumer. Over time, mortgage transactions will shift away from brokers to other channels in order to avoid the increased regulations.

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[37] Zandi, Mark, "House Prices Redux," www.economy.com (October 20, 2002).
[38] 44 U.S.C. Chapter 35 *et seq.*
[39] 5 U.S.C. § 601 *et seq.*

Further, the increased disclosure creates a regulatory (i.e., artificial) competitive disadvantage for mortgage brokers in the marketplace. This disadvantage manifests itself in many ways, from day-to-day operations to how brokers advertise. Indeed, in certain instances, HUD's mandate will not allow a mortgage broker to advertise a "no point" loan, while its competitors may continue to do so.

The Proposed Rule also sets up a new process for originating mortgages called the Guaranteed Mortgage Package Agreement. Created by regulatory fiat, this regime requires an originator to offer a guaranteed mortgage package (mortgage, third party settlement services and closing costs) for a set price. The small business owner is going to be disadvantaged in the marketplace because he or she does not have the bargaining power to enter into volume-based contracts with vendors. The end result will be additional consolidation in the mortgage industry at the expense of small business. This burden will fall disproportionately on small business and is even articulated by HUD – "$3.5 billion of the $6.3 billion in transfers to borrowers comes from small originators ($2.2 billion) such as small brokers and small settlement service providers ($1.3 billion)."[40]

NAMB believes HUD has significantly underestimated the regulatory burden of its Proposed Rule. Indeed, HUD's Paperwork Reduction Act Submissions to OMB states that annual responses for Good Faith Estimates (GFEs) is 11 million.[41] However, HUD's Economic Analysis and Initial Regulatory Flexibility Analysis, states that if the rule applied in the year 2002, it would impact 19.7 million applications.[42] This is significant because the submission to OMB underestimates the paperwork burden by at least 8.7 million GFEs and an additional $57 million.

In addition, HUD's Economic Analysis states that "originators and closing agents will have to expend some minimal effort in explaining to consumers the cross walk between the new streamlined GFE and the more detailed HUD-1."[43] However, this cost is not included in the OMB submission and the cost is not "minimal." NAMB believes a detailed and accurate estimate should be provided.

HUD states that the program change being mandated at HUD would increase burden to industry by 2,530,000 burden hours.[44] This is equal to 289 years. NAMB believes such a huge burden, by definition, will increase the cost of credit to consumers. NAMB also believes this anticipated burden triggers the Unfunded Mandates Reform Act and conflicts with President Bush's recent Executive Order to relieve the regulatory burden on and protect small business.[45]

The Economic Analysis states that $3.5 billion of the $6.3 billion (55%) in transfers to consumers will come from small businesses.[46] NAMB finds this very troubling in the sense that small business – particularly in the housing industry today – is one of the few pillars in this economy that has not fallen. NAMB is concerned that by arbitrarily reducing small business revenues, many will not be able to survive and will therefore reduce consumer choice and access to credit. HUD should ensure that the final

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[40] "Economic Analysis and Initial Regulatory Flexibility Analysis for RESPA Proposed Rule to Simplify and Improve the Process of Obtaining Mortgages to Reduce Settlement Costs to Consumers," U.S. Department of Housing and Urban Development, Office of Policy Development and Research, July 2002, p. vii.
[41] See Exhibit 1, "Supporting Statement for Paperwork Reduction Act Submissions," U.S. Department of Housing and Urban Development, August 2001, p. 5.
[42] "Economic Analysis," p. 9.
[43] *Id.* at p. 25.
[44] "Supporting Statement," p. 7.
[45] Executive Order 13272, August 13, 2002.
[46] "Economic Analysis," p. 26.

regulation will not disproportionately jeopardize the small businessman currently trying to put people in homes.

The Economic Analysis states that the change in characterization of yield spread premiums as stated in the Proposed Rule "will reduce the incomes of those brokers who have been overcharging consumers by receiving a combination of origination fees and yield spread premium payments that is greater than that suggested by competitive markets."[47] What HUD failed to mention in their Analysis is that this will not be the case in connection with FHA and VA-insured loans. As stated later in this letter, under Question 7, those originating FHA[48] and VA-insured mortgage loans are limited to 1% total compensation (or in the case of VA-insured loans, closing costs[49]). In characterizing yield spread premiums as a "lender payment to the borrower," a mortgage broker would not be able to earn enough to cover the cost of originating the mortgage loan. Mortgage brokers will cease originating these loans. As they currently originate approximately 31% of the FHA-insured mortgage loans, additional mortgage brokers will lose additional income.[50]

This and other inconsistencies compel NAMB to ask that HUD undergo a more expansive and realistic review of the economic impact this rule will have on the industry, as well as small business, as mandated by the Regulatory Flexibility Act, the Paperwork Reduction Act, the Unfunded Mandates Reform Act, President Bush's recent Executive Order to relieve the regulatory burden on and protect small business.

NAMB has attached a list of discrepancies with HUD's Economic Analysis to this letter to highlight some of the flaws and inconsistencies. This list is included as Exhibit B to this letter. We ask that the attached document be included for the record.

E. Whether to Rely on the Section 8 Safe Harbor in the Proposed Rule

HUD relies on Section 19 and Section 8(c)(5) of RESPA for its authority in creating a safe harbor from Section 8 liability in exchange for the guarantee of virtually all settlement costs, together with a trackable interest rate, by the packager of these services. Section 19 provides that "the Secretary is authorized to prescribe such rules and regulations, to make such interpretations and to grant such reasonable exemptions for classes of transactions, as may be necessary to achieve the purposes of this Act."[51] Section 8(c)(5) provides that "Nothing in this section shall be construed as prohibiting: ... (5) such other payments or classes of payments or other transfers as are specified in the regulations prescribed by the Secretary, after consultation with the Attorney General, the Secretary of Veteran's Affairs, the Federal Home Loan Bank Board, the Federal Deposit Insurance Corporation, the Board of Governors of the Federal Reserve System, and the Secretary of Agriculture."[52] While this could provide the necessary authority for providing a safe harbor from Section 8 liability, NAMB expresses concern that HUD's reliance on these provisions will be challenged in the courts as to its validity.

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[47] "Economic Analysis," p. 87.
[48] 24 C.F.R. § 203.27.
[49] 38 C.F.R. § 36.4312.
[50] Letter from Engram A. Lloyd, Director, Philadelphia Homeownership Center, Department of Housing and Urban Development, to Paul H. Scheiber, Blank Rome Comisky & McCauley LLP on 8/12/2002.
[51] 12 U.S.C. § 2617(a).
[52] 12 U.S.C. § 2607(c)(5).

Kickbacks and referral fees have been prohibited since the enactment of RESPA. Originally Section 7 of the RESPA, the legislative history states that "by dealing directly with such problems as kickbacks, unearned fees, ... the Committee believes that S. 3164 will ensure that the costs to the American home-buying public will not be unreasonably or unnecessarily inflated by abusive practices."[53] This express prohibition has remained in place since 1974. While HUD is provided certain authority to provide for exemptions, recent caselaw declares that deference is not always provided to an agency interpreting statutory provisions.

In *Pfennig V. Household Credit Service, Inc. and MBNA America Bank, N.A.*, the United States Court of Appeals for the Sixth Circuit found that although language in Regulation Z specifically excluded certain costs from the finance charge, the fees were within the statutory definition contained in the Truth in Lending Act and thus must be included in the calculation of the finance charge.[54] The court stated that the failure "to accurately represent the finance charge contravenes TILA's statutory goal of providing adequate disclosure in order that the consumer will knowledgeably be able to compare credit options and 'avoid the uninformed use of credit.'"[55] As such, here is an instance where an agency clearly has the authority to prescribe regulations implementing the statute[56] but the court found that it must still prescribe to the language of the statute. Further, could a court of law find that HUD's Proposed Regulation, if finalized, in contravention of the goal of RESPA, "the elimination of kickbacks or referral fees that tend to increase unnecessarily the costs of certain settlement services?"[57] Similar to this case, and in light of these circumstances, as the language of RESPA does prohibit these practices, it would seem risky to rely on HUD's safe harbor only to be challenged in court.[58]

Further, it is unclear whether a mortgage broker who utilizes a third party's package would be exempt from any Section 8 liability under HUD's Proposed Rule. While it is clear that those within the package and the packager fall within the exemption, it is unclear whether a mortgage broker using a wholesale lender's package would be able to claim the safe harbor as well. Thus, it seems unlikely that a mortgage broker would rely on this exemption as he or she might rely on it to their detriment.[59]

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[53] 12 U.S.C. § 2606 (1974).

[54] *Pfennig v. Household Credit Services, Inc. and MBNA America Bank, N.A.*, 2002 FED. App. 0123P (6th Cir.).

[55] *Id.*

[56] The Federal Reserve Board has the authority "to prescribe regulations to carry out the purposes" of TILA. 12 U.S.C. § 1604(a).

[57] 12 U.S.C. § 2601(b)(2).

[58] NAMB's fear of class action lawsuits, together with other lawsuits, is not misplaced. In the past ten years, class action lawsuits have been filed over courier fees, yield spread premiums, document preparation fees, and the "up charging" of third party fees. These lawsuits have cost the industry thousands of dollars, if not millions, in liability.

[59] NAMB understands that RESPA provides that "no provision of this Act or the laws of any State imposing any liability shall apply to any act done or omitted in good faith in conformity with any rule, regulation, or interpretation thereof by the Secretary or the Attorney General, notwithstanding that after such act of omission has occurred, such rule, regulation, or interpretation is amended, rescinded, or determined by judicial or other authority to be invalid for any reason." 12 U.S.C.§ 2617(b). However, as was seen in *Pfennig v. Household*, this did not stop the litigation.

VI. Specific Requirements will Open Originators and other Participants to New Areas of Litigation and Potential Liability

A. The New Disclosure Forms Require the Disclosure of the Annual Percentage Rate

The calculation and disclosure of the annual percentage rate is required under the Truth in Lending Act, which is regulated by the Federal Reserve Board. Currently, mortgage brokers (non-tablefunding mortgage brokers[60]) are not required to calculate and disclose the annual percentage rate to consumers. The Truth in Lending Act requires that creditors provide a disclosure containing the annual percentage rate of the loan (as defined in the Act), as well as certain other prescribed information to consumers.[61] A "creditor" is defined as "a person (A) who regularly extends consumer credit that is subject to a finance charge or is payable by written agreement in more than four installments (not including a downpayment), and (B) **to whom the obligation is initially payable, either on the face of the note or contract** [emphasis added], or by agreement when there is no note or contract."[62] As traditional mortgage brokers are not considered "creditors" under the Truth in Lending Act, they are not required to calculate the annual percentage rate or disclose it to consumers. HUD's definition of a mortgage broker[63] is much more expansive than the Federal Reserve Board's definition under the Truth in Lending Act and certain tablefunding mortgage brokers may or may not be required to disclose the annual percentage rate to consumers. Thus, HUD would be subjecting mortgage brokers to a disclosure requirement that the law itself, and its implementing regulations, does not subject mortgage brokers to unless the mortgage broker is tablefunding the transaction.

The calculation of the annual percentage rate is one of the more difficult functions performed by an originator – not the calculation itself, rather there is difficulty in determining which fees must be included in the calculation. The Truth in Lending Act, and its implementing regulations, Regulation Z, even provide for tolerances to ensure that an originator has a harmless margin of error. One remembers a recent series of class action lawsuits brought for failure to include a courier fee in the calculation of the finance charge (upon which the annual percentage rate is based).[64] These class action lawsuits were so potentially industry threatening that Congress placed a moratorium on the lawsuits until the issue could be solved. HUD would be subjecting mortgage brokers to a new threat of litigation and a potential new area of liability. Further, it would be subjecting mortgage brokers to this threat when Congress and the Federal Reserve Board both deemed it appropriate not to subject mortgage brokers to this requirement.

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[60] NAMB is using the term "non-tablefunding mortgage brokers" to mean mortgage brokers who originate mortgage loans in which the broker is not initially payable on the face of the note and are not using their own funds to fund the mortgage loan.
[61] 12 C.F.R. § 226.17(a)(1).
[62] 12 C.F.R. § 226.2(17).
[63] HUD defines a mortgage broker in the Proposed Rule as "a person (not an employee of a lender) who table funds or acts as an intermediary in a federally related mortgage loan. Mortgage brokers that are the real source of funds for a federally related mortgage loan are not regarded as brokers in such transactions." Proposed Rule, Fed. Reg. at 49,134.
[64] *Rodash v. AIB Mortgage Co.*, 16 F.3d 1142 (11th Cir. 1994).

B. The New Disclosure Forms Require a Transaction Specific Chart Detailing Different Methods of Payment

Currently, the HUD proposed rule requires originators to create a "sample" chart, on a loan-by-loan basis, that would provide the consumer with comparisons of the options available for payment of settlement costs to lower the consumer's interest rate. However, the volatility of the marketplace renders this requirement virtually untenable. An originator will have difficulty in complying with this requirement as the market changes too rapidly for a loan originator in the field to create in the manner contemplated in the proposed rule. Further, any error committed by an originator in completing this chart, especially for mortgage brokers in the field, will be an invitation to litigation for attorneys.

NAMB, however, sees the utility for consumers to have some information for comparison and for the purposes of "shopping." As such, we find a workable middle ground to be the inclusion of a generic "sample" chart.

C. Failure to Meet the Requirements, Even Due to Harmless Error, under the Enhanced Good Faith Estimate or the Guaranteed Mortgage Package Agreement

The Proposed Rule provides that under the enhanced good faith estimate scheme, "if the cost at settlement exceeds the estimate reported on the good faith estimate, absent unforeseeable and extraordinary circumstances, the borrower may withdraw the application and receive a full refund of all loan-related fees and charges."[65] Further, the proposed rule provides that under the guaranteed mortgage package agreement, in order to qualify for the limited Section 8 exemption, an entity must comply with all requirements for the provision of the Guaranteed Mortgage Package Agreement.[66] Both of these requirements leave no room for a right to cure in the case of harmless error on the part of the originator. This seems to be an open invitation to litigate on the part of consumers.

VII. Specific HUD Questions on the New Good Faith Estimate (GFE) Requirements

1. As proposed in Section III.A.(1), the proposed GFE form would briefly explain the originator's functions and that the borrower, not the originator, is responsible for shopping for his or her best loan. Does this language adequately convey this message? If the commenter thinks otherwise, it should provide alternative language for the form that better explains the loan originator's function to the borrower. Should the form also address agency requirements under state laws and how?

In several states, such as California[67] and New York, a mortgage broker has a statutory fiduciary duty to its customers. Also, in certain states, such as Minnesota,[68] an originator may choose to act as the agent of the consumer. Thus, in these instances, this language is not appropriate. NAMB suggests that the language state:

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[65] Proposed Rule, Fed. Reg. at 49,159.
[66] Proposed Rule, Fed. Reg. at 49,160.
[67] Cal. Bus. & Prof. Code § 10229(q); Cal. Fin. Code § 4979.5a; Cal. Fin. Code § 50701(c).
[68] Minn. Stat. § 58.15.2.

We agree to perform or provide services, goods or facilities to assist you in the origination of a mortgage loan. The services, goods or facilities may be performed or provided for your direct benefit, or some of them may benefit you only indirectly, in that they are performed on behalf of third parties (e.g., wholesale lenders or secondary market investors) but are necessary to the objective of obtaining the mortgage loan you desire. While we seek to assist you in meeting your financial needs, we cannot guarantee the lowest price or best terms available in the market. We, as with all originators, may not offer all the products that are available in the marketplace.

2. **In Section III.B.(2) c., the proposed rule requires that the amounts estimated on the GFE for mortgage broker and lender origination charges may not vary at settlement absent unforeseeable circumstances. Should the rule provide for this "unforeseeable circumstances" exception? Are the particular circumstances specified in HUD's formulation in this proposal sufficiently encompassing? What evidence should a broker or lender be required to retain to prove the existence of such circumstances and justify any increase in charges at settlement?**

   and

3. **In Section III.B.(2).c., the proposed rule establishes a 10% limit, or "tolerance," for categories of settlement services and costs including third party services that the borrower shops for and escrow/reserves by which such costs cannot exceed the GFE estimates by 10% at settlement absent unforeseeable and extraordinary circumstances. It also establishes zero tolerances for origination charges and lender required lender selected third party costs and government charges that cannot vary from estimate through settlement absent unforeseen circumstances. Are those appropriate tolerances and tolerance levels or should other tolerances/tolerance levels be established for these categories? Also, should a tolerance be established for borrower's title insurance? What alternative or additional means might be employed to ensure that loan originators take the care necessary to complete the GFE to ensure that it represents a Good Faith Estimate of final settlement costs?**

Congress required, in its passage of amendments to RESPA in 1975, that "each lender shall include with the booklet a good faith estimate of the amount or range of charges for specific settlement services the borrower is likely to incur in connection with the settlement as prescribed by the Secretary."[69] HUD bases its authority for creating the fee guarantees and tolerances (in connection with the good faith estimate) upon this solitary statement. Again, NAMB believes that HUD should seek legislative authority in any strengthening of the good faith estimate of settlement costs.

However, that said, NAMB could not support the guarantee or tolerance provisions for third party fees contained in the proposed rule. Third party fees are beyond the control of the originator and thus should not be required to be guaranteed or subject to a very low tolerance within three (3) business days of application. Loan originators have little control over third party service providers. For example, a title insurer may cease honoring pending contracts for title examination services. A loan originator who contracted with the insurer to provide title services to a consumer would now have to act quickly to replace the insurer with another provider. This provider might not be open to meeting the contracted-for price. An originator would then be forced to lose this money. While it is neither the fault of the

[69] 12 U.S.C. § 2604(c).

originator or the consumer, the originator should not be held accountable for this increase in a third party fee expense. Consider when a wholesale lender requires additional comparisons on an appraisal – should the mortgage broker be held responsible? Unfortunately, the exemption provided for in the proposed rule does not allow for these circumstances and any number of other circumstances. This could seriously harm a small business – of which most mortgage brokers are – and threaten their very existence.

Finally, any third party charge that is not selected by the originator should not be subject to a tolerance within three (3) business days of application. For example, many states require an originator to allow a consumer to choose certain third party settlement service providers.[70] This is consumer's responsibility to choose and an originator should not be responsible for estimating these fees.

In reference to the exception provided for in the Proposed Rule, "unforeseeable and extraordinary circumstances," this is an extremely high standard that does not take into account certain valid reasons for increasing or decreasing the amount of compensation received by an originator or third party settlement costs. We propose that HUD include several other exceptions to this standard, such as instances where the borrower is not eligible for a loan program based upon underwriting guidelines, the borrower asks that the loan program or loan amount be changed, a consumer is not eligible for the loan program applied for, the property offered to secure the loan changes or does not qualify, or a different pricing option is chosen.

Another exception that should be included is any instances of borrower fraud. HUD appears to gloss over the issue of borrower fraud and its impact on the industry. A recent informal survey performed by Advantage Credit "found that 23% of mortgage brokers said they received an application that contained intentionally fraudulent statements from a borrower."[71] Originators faced with fraudulent applications from borrowers might be unconscionably held to certain terms and fees disclosed in the good faith estimate.

It is a great responsibility buying a home. It is the largest financial transaction in which the majority of Americans will ever engage. However, the laws should not extend so far in one direction so as not to infuse responsibility on the consumer for the transaction. Every mortgagor should be beholden to educate themselves so as not to become a "victim." In guaranteeing virtually all mortgage fees, the only risk being borne is borne by the originator.

NAMB would support the guarantee of all originator costs to a consumer with certain exceptions that are predicated on the eligibility and consumer choice (as stated above). As an alternative to creating a tolerance for third party fees, NAMB can support a redisclosure requirement. This redisclosure requirement could be required for a period of time prior to settlement, which will allow the consumer time to find another originator should they choose not to accept the disclosure of fees. This should eliminate surprise at settlement while allowing the originator adequate time to underwrite the proposed loan to ensure that the fees disclosed are adequate representations of the amounts to be charged to the consumer.

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[70] As stated above, as an example, in Maryland, under certain conditions, a consumer may choose their own title insurance provider. Md. Code Ann., Com. Law II §§ 12-1028(c)(1) and 12-119(b).

[71] National Mortgage News, September 1, 2002.

4. In Section III.B.(2) d., the proposed rule would amend Regulation X to make clear that loan originators may enter into volume arrangements where such discounted prices are charged to their customers. Commenters are invited to provide their views on the ramifications, if any, of this clarification.

Volume discounts for settlement services that are passed through to the consumer are not currently a violation of Section 8. Thus, an originator can negotiate volume discounts with settlement service providers if the savings are provided to the consumer in the form of lower costs. However, there seems to be little incentive for doing so. Section 8 litigation has become a cottage industry for certain class action attorneys and as such poses a significant economic risk to loan originators. Further, with two courts holding that a settlement service provider may mark up third party settlement service charges without violating Section 8(b) of RESPA, there seems to be a patchwork of regulation in this area.[72]

Finally, it seems that HUD would find it difficult to enforce instances in which the savings were not passed to the consumer. As HUD does not routinely perform audits or examinations of mortgage originators in this country (with the exception of FHA mortgagees), a complaint must be lodged first to trigger an investigation. This would render enforcement of these arrangements very difficult. Thus, it seems unlikely that a mortgage originator will determine that the risk is balanced by the advantages gained by entering into volume-discounts.

5. In Section III.B.(2) c., the proposed rule requires that the tolerances will apply to the GFE from the time the form is given by the loan originator through settlement. Also, in case it takes a substantial time for the borrower to decide to use the loan originator from the date the form is given, the rule and the form provide that the GFE need only be open for borrower acceptance for a minimum of 30 days from when the document is delivered or mailed to the borrower. After that time, the GFE could be ratified or superseded by the originator at the borrower's request. Is this expiration date appropriate to protect against unnecessary costs flowing from an indeterminate liability or for other reasons? Is 30 days too long or too short? Another possibility that commenters may consider is whether the numbers on the GFE should apply only from the time the borrower enters into an agreement with the loan originator. HUD also invites commenters' views on whether HUD now should require a borrower's signature on the GFE to memorialize acceptance and begin the period during which the estimates are binding.

NAMB can support providing the consumer with a guarantee of originator fees for seven (7) days, during which time the consumer may shop among originators. At the end of the seven days, or at any time during this seven-day (7) period, a consumer may choose to accept the loan and move forward through the origination process. However, NAMB does not support a seven-day (7) availability for third party fees and additional fees as we detailed above. These fees are frequently beyond the control of the originator and thus cannot be guaranteed. The disclosure of these fees is discussed above.

Please note that NAMB believes that the volatility of the marketplace prevents comparing a good faith estimate to one prepared thirty (30) days later. It would be similar to comparing apples and oranges. This would not be amenable to a consumer shopping. Further, while HUD believes this will increase

[72] *Boulware v. Crossland Mortgage*, No. 01-2318 (4th Cir.), (May 22, 2002) and *Echevaria v. Chicago Title & Trust Company*, No. 00-4087 (11th Cir.), (July 5, 2001).

competition and drive settlement prices to decrease, some originators will be less likely to negotiate discounts with third party service providers for fear of Section 8 litigation, whether warranted or not. Finally, this also provides some level of protection for the originator from borrowers fraudulently preparing false good faith estimates.

Finally, the thirty (30) day period might conflict with ECOA and Regulation B. Regulation B requires that a creditor[73] notify an applicant of action taken within thirty (30) days after receiving a completed application concerning the creditor's approval of, counteroffer to, or adverse action on the application (among others).[74] Depending on how much information a creditor has at the time it provides the consumer with the disclosure, these two time periods might directly conflict with each other.

6. **In Section III.B.(1) b.; the proposed rule simplifies the GFE by placing all loan origination costs in a small number of primary categories. This is intended to facilitate borrower understanding and shopping of major loan costs and minimize the proliferation of "junk fees" and duplicative charges. How could the GFE be made even simpler to facilitate borrower shopping? If the commenter believes greater itemization is desirable, what should be itemized and why?**

NAMB does not believe that the enhanced good faith estimate form provided for in the proposed rule will facilitate borrower understanding and shopping of major loan costs and minimize the proliferation of "junk fees" and duplicative charges. Rather, this form is confusing and busy and will only prove a disservice to the consumer. NAMB has created an alternative form for use in connection with the good faith estimate that is attached as Exhibit A to this comment letter. We believe that this form is more clear, provides the information in a simple fashion that a consumer needs in order to shop for a mortgage loan yet provides detailed information where necessary. Further, it provides a disclosure of yield spread premiums in a manner that is more in keeping with the "definition" provided for in HUD's Statements of Policy 1999-1 and 2001-1. NAMB has also incorporated several elements contained in the Proposed Rule into its proposed disclosure.

Finally, NAMB supports the continued itemization of fees for several reasons: (i) borrowers will continue to ask what comprises the origination costs as well as the settlement costs; (ii) this will provide consumers with more information in order to compare the good faith estimate to the HUD-1; (iii) provides for less conflicts with state law; and (iv) others.

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[73] As defined under Regulation B.
[74] 12 C.F.R. § 202.9(a)(1)(i).

7. **In Section III.A.(3), the proposed rule requires that on the front of the proposed form mortgage brokers disclose the lender credit right below the total origination charges to: (a) Make the borrower aware of the effect that the credit has to reduce total origination costs; (b) avoid confusion among borrowers; and (c) avoid giving any competitive disadvantage to either a broker or a lender for the same loan. What, if any, other approach to address these concerns is better and why? Should the new GFE form disclose this credit at the bottom of the proposed form because the credit can be applied to all settlement costs?**

Characterizing yield spread premiums as a lender payment to the borrower creates *unintended consequences* and *provides less clarity* to consumers than as presently disclosed. In the Proposed Rule, HUD seeks meaningful disclosure of mortgage broker fees to borrowers. However, the proposed method of disclosure achieves just the opposite – it muddies the waters as to how indirect broker compensation works in reality. Under the proposed structure, indirect broker compensation is disclosed as a "lender payment to the borrower for higher interest rate."[75] Not only is this inflammatory, it seems to discount HUD's own Statement of Policy, in which it states that yield spread premiums can be payments for goods, services, and facilities provided to the lender by the mortgage broker. NAMB believes that HUD's characterization of yield spread premiums creates a multitude of problems, not the least of which is a new round of class action lawsuits.

As described above, HUD's characterization of yield spread premiums contradicts HUD's own statements in Statement of Policy 2001-1. This characterization does not provide a level playing field for all originators in that lenders who sell loans on the secondary market are not required to disclose the compensation received by them when they sell the loan. While we understand that HUD does not believe that it has the authority to require such disclosure by lenders, NAMB believes that as level a playing field as can be generated is necessary for all originators to remain competitive. As we stated above, we believe that HUD agrees with this statement; in the 2001 Policy Statement HUD states that "the department strongly believes that all lenders and brokers should provide the level of consumer disclosure that the purposes of RESPA intend and that fair business practices demand [emphasis added]."[76] As such, NAMB supports the inclusion of language notifying consumers that this type of compensation is paid to lenders, although we understand that HUD cannot require the amount of this compensation to be paid.

The proposed characterization, as stated in the above paragraph, places mortgage brokers on an unlevel playing field with other originators. First, many mortgage brokers will no longer be able to originate FHA and VA-insured mortgage loans. [77] Direct originator compensation on these loans is limited to 1% of the loan amount in connection with FHA-insured mortgage loans, while direct originator compensation on VA-insured mortgage loans is limited to 1% of the total loan amount or closing costs. These loans are difficult to originate due to the many additional documentation requirements (on average an additional six to ten pages of additional documentation is required), as well as the fact that many FHA-mortgagors are

[75] Proposed Rule, Fed. Reg. at 49,164.
[76] Statement of Policy 2001-1, Fed. Reg. at 53,057.
[77] This is significant as approximately 31% of all FHA loans are originated by mortgage brokers. Letter from Lloyd to Scheiber 8/12/2002. A recent trade press article stated that "Federal Housing Administration one- to four-family loan originations jumped 25.7% to a record $148.0 billion in fiscal year 2002, which ended Sept. 30. FHA loan endorsements totaled 1.29 million -- the third-best year ever." National Mortgage News, October 17, 2002. Further, this article stated that "in fiscal 2001, the FHA endorsed 1.01 million loans totaling $117.7 billion, according to the Department of Housing and Urban Development." *Id.*

credit impaired, first time homebuyers, or non-traditional consumers and thus need more time spent with them in answering questions and concerns.

Many mortgage brokers, in order to be compensated for the time and work involved in the origination of these loans, rely on yield spread premiums to cover these costs. In characterizing yield spread premiums as lender payments to the borrower, indirect compensation is transformed into direct compensation and thus subject to the cap. Many mortgage brokers will cease to originate FHA and VA-insured loans. This will impact many first time homebuyers who rely on FHA and VA-insured mortgage loans for their low downpayment requirements and force these consumers into subprime loans. This is significant as approximately 31% of all FHA-insured mortgage loans are originated by mortgage brokers.[78] Further, a recent trade press article stated that "Federal Housing Administration one- to four-family loan originations jumped 25.7% to a record $148.0 billion in fiscal year 2002, which ended Sept. 30. FHA loan endorsements totaled 1.29 million -- the third-best year ever."[79] Further, this article stated that, according to the Department of Housing and Urban Development, "in fiscal 2001, the FHA endorsed 1.01 million loans totaling $117.7 billion."[80]

Further, if the proposed characterization of yield spread premiums is implemented, mortgage brokers will not be able to advertise certain mortgage loans and remain competitive. For example, a mortgage broker who makes a "no point" mortgage loan at 7% interest rate on a $100,000 loan, but collects a $1,000 yield spread premium, must advertise that this is a one-point mortgage loan. A mortgage lender, who originates a $100,000 mortgage loan at a 7% interest rate, but collects $1,000 in compensation when the loan is sold, can advertise a "no-point" loan. These are the same loans and same costs to the consumer but the mortgage broker appears more expensive as he or she must advertise that this is a one-point mortgage loan. Thus, mortgage brokers will appear less competitive.

Characterizing a yield spread premium as a direct payment to the borrower will also impact certain predatory lending laws. Many state laws incorporate the Federal Reserve Board's definition of "points and fees."[81] Under the federal Home Ownership and Equity Protection Act (HOEPA), and implementing regulations, Regulation Z Section 32, the definition of "points and fees" includes "all compensation paid to mortgage brokers."[82] The commentary to the Truth in Lending Act specifically excludes "mortgage broker fees that are not paid by the consumer."[83] Under the new characterization of yield spread premiums, this amount will be paid by the consumer to the mortgage broker. Not only might this capture more loans, such as certain conforming loans, under HOEPA, but yield spread premiums will in essence be double counted as they are already included in the interest rate. Many loans that have no need for the added protections afforded high cost loans, such as conforming loans, will fall under these laws. Consumers will lose valuable choice as certain loan products are not available under these laws, such as balloon payment loans or prepayment penalty products.

[78] Letter from Lloyd to Scheiber on 8/12/2002.
[79] National Mortgage News, October 17, 2002.
[80] *Id.*
[81] Three recent examples include the following: Florida Senate Bill 2262, Colorado House Bill 1259, and Maryland Senate Bill 649.
[82] 12 C.F.R. § 226.32(b)(1)(ii).
[83] Regulation Z Commentary § 226.32(b)(1)(ii).

Consumers will also be disadvantaged in other ways. NAMB is unsure if HUD's characterization will require the provision of a 1099 form to consumers will be necessary as the lender will be paying money to the consumer. This could potentially trigger additional tax consequences for consumers.

Mortgage brokers maintain contracts with wholesale lenders with whom they transact business. These contracts require that a mortgage broker refund the money received from a mortgage lender if the loan is refinanced within a certain time frame. This helps to ensure that an unscrupulous mortgage broker does not engage in loan flipping in order to earn more profit. These contractual obligations will be unenforceable as the mortgage broker receives all of its compensation from the consumer. The mortgage lender will be forced to seek compensation from the consumer, which appears senseless. Further, this will be one less check against an unscrupulous mortgage broker.

Finally, indirect compensation should not be characterized in the proposed rule as "a payment for a higher interest rate." This is inflammatory and does not fully explain the purpose of a yield spread premium. HUD discusses in two Statements of Policy that yield spread premiums are not per se illegal, if the total mortgage broker compensation is for goods or facilities provided or services performed and the total compensation to the mortgage broker is reasonably related to the total set of goods or facilities actually furnished or services performed.[84] Further, these goods, facilities or services could be provided by the mortgage broker to both the lender and the borrower.[85] This would negate the proposed characterization of yield spread premiums and where the information is disclosed on the form.

NAMB supports the disclosure of yield spread premiums on the good faith estimate more in keeping with the two Statements of Policy issued by HUD – a lender payment to the mortgage broker for goods, facilities and services. This disclosure will be more accurate based upon the two-part test contained in Statement of Policy 1999-1 and 2001-1. Further, as HUD confirms in the Proposed Rule, a yield spread premium can be payment to the mortgage broker for services provided to the borrower and the lender.[86]

Further, NAMB proposes that the disclosure of yield spread premiums be disclosed as "compensation for goods, facilities and services." This reflects that indirect compensation may be paid to the mortgage broker for goods, facilities, and services performed for both the borrower and the lender. In NAMB's proposed form, which is attached to this letter as Exhibit A, we suggest that the following language be utilized to describe the yield spread premium: "An originator may be compensated by an investor for goods, facilities or services provided to you or to the investor. This will result in a higher interest rate for this loan. If you would rather pay less cash up front, you may be able to pay some or all of the originator's compensation indirectly through a higher interest rate. If you would rather have a lower interest rate, you may pay higher up-front points and fees. This amount will not exceed the amount disclosed to the left of this description. If the originator is acting as a lender in this transaction, the originator may receive additional compensation when it sells the loan for the value of the servicing rights or the value of the interest rate or a combination of both. This amount is not required to be disclosed."

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[84] Statement of Policy 2001-1, Fed. Reg. at 53,052.

[85] As stated earlier in this letter, HUD states in the background on the proposed rule that "as retailers, brokers also provide the borrower **and the lender** [emphasis added] with goods and facilities such as reports, equipment, and office space to carry out retail functions." Thus, characterizing yield spread premiums as lender payments to the borrower is inaccurate as the lender may compensate the mortgage broker for providing brick and mortar, and other goods and facilities. In utilizing mortgage brokers, wholesale lenders can provide mortgage loan products at conceivably lower rates and lower costs to consumers.

[86] See above.

8. As proposed in Section III.A.(3), as another step to avoid borrower confusion and any competitive disadvantage among lenders and brokers, the proposed rule breaks out on Attachment A-1, rather than on the front of the proposed form, the "Loan Origination Charges" into "Lender Charge" and "Broker Charge." How, if at all, does this approach advantage or disadvantage either lenders or brokers or confuse borrowers in comparison shopping? Would the industry and borrowers be better served if there is a breakout of "Lenders Charges" and "Broker Charges" on the front of the form and why?

NAMB supports the continued itemization of fees on the good faith estimate. This will assist in eliminating conflicts with certain state laws. For example, California requires that a mortgage broker provide consumers with a Mortgage Loan Disclosure Statement. This statement requires that certain fees be itemized.[87] Thus, a consumer will have continuity between certain state required forms and federal disclosures.

In not itemizing origination and settlement costs, the disclosure will also conflict with the federal Truth in Lending Act. Under this Act, a creditor is required to provide an itemization of the amount financed together with its annual percentage rate disclosure.[88] Thus, consumers will be provided a disclosure that itemizes certain costs of the mortgage loan regardless of whether HUD desires it so.

However, NAMB does not agree with breaking down the charges into "Lender Charges" and "Broker Charges." This could present an unlevel playing field for mortgage brokers. Rather, NAMB proposes that the fees be broken down into "Origination Costs," which represents all direct compensation paid to a mortgage broker and a mortgage lender, and "Settlement Costs," which are all third party fees required for settlement of the mortgage loan. These fees NAMB proposes be disclosed on the first page of its proposed form, as attached as Exhibit A. This is clearer to consumers than breaking down the fees into "Broker Charges" and "Lender Charges." Further, it places no originator at a disadvantage. Finally, this should prove to be more useful as a shopping tool for consumers.

9. As proposed in Section III.B.(2) e, the new GFE will consolidate certain charges into lump sum categories (e.g. lender required third party services). To permit the borrower to compare the new GFE to the HUD-1, it will be necessary for HUD to establish additional instructions to guide the reader so that the new GFE could be compared to the HUD-1. Would it be better to change the HUD-1 so the fee categories correspond to the groupings on the GFE and the two documents can be more easily compared? If commenters support changes to the HUD-1 to make it more comparable to and compatible with the new GFE, how extensive should these changes be and in what areas? Should the HUD-1 continue to list all charges for services or should it also be shortened and simplified as well to cover only categories of service?

HUD identified one of the guiding principles of RESPA reform as simplification of the loan origination process. The rule amends the good faith estimate significantly yet provides no corresponding amendments to the HUD-1 or HUD-1A Settlement Statements. In the proposed rule itself, HUD admits that "the proposed new GFE ... is not readily comparable to either the HUD-1 or HUD-1A form."[89]

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[87] Cal. Bus. & Prof. Code § 10241.
[88] 12 C.F.R. § 226.18(b).
[89] Proposed Rule, Fed. Reg. at 49,151.

HUD did not amend the HUD-1 (with the exception of minor changes to the instructions) as it states that the HUD-1 "is well accepted as a listing of settlement service charges by industry and consumers alike."[90] However, this does not seem to benefit the consumer. Corresponding changes to the HUD-1 should be effected for any changes enacted to the good faith estimate. Otherwise, consumers will find it difficult to compare the two documents.

If any changes to the good faith estimate form currently utilized by industry are effected, corresponding changes should be made to the HUD-1 Settlement Statement. The HUD-1 should be amended to reflect the changes made in the good faith estimate, such as groupings of settlement and origination costs. Also, the HUD-1 should continue to include an itemization of the costs, as discussed in NAMB's response to Question 8.

10. Should a safe harbor from Section 8 scrutiny be established for transactions where the mortgage broker signs and contractually commits to its charges on the GFE? The purpose of proposing this safe harbor would be to encourage a firm contractual commitment to borrowers, before they pay a fee and commit to a particular mortgage broker, so that the borrower can shop among mortgage brokers. Considering the proposed changes to the GFE, the proposed packaging safe harbor and HUD's current guidance on mortgage broker fees, is this safe harbor necessary for industry or borrowers and why? In light of the proposed rule's other provisions is any other additional disclosure for mortgage brokers warranted, such as an additional statement of what the broker's fees are and how they functions?

NAMB supports the guarantee of "origination costs" (as defined in NAMB's proposal as all fees paid by the consumer to the lender or the mortgage broker) under the good faith estimate, with certain exceptions, as described above. However, NAMB supports the estimation of all other costs. As stated above, third party costs are beyond the control of an originator and should not be included in any guarantee. Thus, in the area of origination costs, where it appears, at least anecdotally, most of the abuses occur, a mortgage broker will be obligating itself to these costs, with certain exceptions.

It seems that the Statement of Policy 2001-1 has finally put to rest class action lawsuits in connection with yield spread premiums. HUD has stated, and many courts have agreed that yield spread premiums are not illegal per se and must be subjected to HUD's two part test iterated in Statement of Policy 1999-1 and clarified in Statement of Policy 2001-1.

In NAMB's proposal, we have included statements that discuss what a yield spread premium is and how they function. This language is as follows: "An originator may be compensated by an investor for goods, facilities or services provided to you or to the investor. This will result in a higher interest rate for this loan. If you would rather pay less cash up front, you may be able to pay some or all of the originator's compensation indirectly through a higher interest rate. If you would rather have a lower interest rate, you may pay higher up-front points and fees. This amount will not exceed the amount disclosed to the left of this description. If the originator is acting as a lender in this transaction, the originator may receive additional compensation when it sells the loan for the value of the servicing rights or the value of the interest rate or a combination of both. This amount is not required to be disclosed." NAMB believes that

[90] Proposed Rule, Fed. Reg. at 49,152.

this information, together with the discussion on "Interest Rate and Settlement Costs Options" and the generic chart provide the consumer with considerable information on indirect broker compensation.

VIII. Specific HUD Questions on the Guaranteed Mortgage Package Agreements (GMPA)

11. Is a safe harbor along the lines proposed in Section III. C. (1) of this rule necessary to allow lump sum packages of settlement services to become available to borrowers? Would the proposed clarification by HUD that discounts may be arranged, if passed on to borrowers and not marked up, suffice to make packages available to borrowers? Would a rule change to approve volume discounts and/or markups when a package is involved suffice? Would it suffice to trim the disclosure requirements for packaging and offer the option of providing a streamlined GFE to those who packaged?

NAMB does not believe that a safe harbor as described in the proposed rule is necessary for the packaging of settlement services for consumers. Certain lenders already package settlement services and provide these guaranteed costs to consumers.[91] The market will demand these guaranteed packages if it has an appetite for it. By providing a safe harbor from Section 8 liability, HUD will be encouraging packagers to increase the cost of the package, in order to cover any losses, with no repercussions for the packager. In other words, without Section 8 liability, a packager may arbitrarily increase its price with no remedies for the consumers. While this may appear to drive down costs initially, NAMB foresees it only leading to an increase in costs as the remaining larger entities can also draw on their new found monopoly in the market that packaging has created.

Further, NAMB believes that HUD's codification of its longstanding opinion that an originator may arrange volume discounts for settlement services if the discounts are passed on to consumers will provide originators with the sufficient security to offer these discounts to consumers. The market will demand these lower prices from originators but all will be able to compete.

NAMB is interested in any responses HUD has received from other agencies in connection with the proposed Section 8 exemption for packaging. RESPA requires that HUD must consult with the Attorney General, the Secretary of Veterans' Affairs, the Federal Home Loan Bank Board, the Federal Deposit Insurance Corporation, the Board of Governors of the Federal Reserve System, and the Secretary of Agriculture prior to exempting any "payments or classes of payments or other transfers."[92] There is no mention in the Proposed Rule of HUD's contact with these agencies or their comments regarding this exemption.

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[91] Mortgage.com, the website for retail originations for ABN AMRO Mortgage Group, Inc., currently packages settlement costs for consumers. These guaranteed package prices, which are available on the website www.mortgage.com, are available together with an interest rate for consumers. Certain of settlement service fees are contained in the package price.
[92] 24 U.S.C. § 2607(c)(5).

12. As proposed in Section III. C. (6) is the scope of the safe harbor appropriately bounded in applying to all packagers and participants in packages? The safe harbor also currently does not apply to referrals to the package. Should there also be a bar against part time employees of other providers working for the package to steer business? How should the safe harbor apply to affiliated business arrangements to protect borrowers from steering?

Part time employees of other providers should be barred from steering consumers to a certain package created by their employer. For example, a loan originator who works part time for a third party settlement service provider should be barred from steering consumers toward their company's package. Certain individuals exert a special sort of influence and steering might occur due to this influence. If one of the goals of packaging is shopping, it seems contradictory to not prohibit steering. This applies to affiliated business arrangements as well.

There seems to be incentive for a non-packager, such as a mortgage broker or third party settlement service provider, to utilize a third party's package when no Section 8 exemption pertains to them. This statement does not in any way negate NAMB's belief that packaging will greatly disadvantage small business and leave them unable to compete.

13. As proposed in Section III. C (5), to qualify for the safe harbor, the packager must include an interest rate guarantee with a means of assuring that when the rate floats, it reflects changes in the cost of funds not an increase in originator compensation. For this purpose, the rule suggests tying the rate to an observable index or other appropriate means. What other means could assure borrowers that the rate of a lender was not simply being increased to increase origination profits? For example, would a lender's commitment to constantly make rates public on a web site be a useful control? If an index is the best approach, how should it be set? If an index approach is approved, should each lender be allowed to pick its own observable index?

In NAMB's meetings with industry representatives, consumer advocates, and GSE representatives on mortgage reform over the past several years, many hours have been spent in attempting to produce a single index that a consumer may use to track interest rates. Members of our Association distinctly remember being part of meetings where representatives of Fannie Mae, Freddie Mac, and Wall Street investment companies stated that there was no one index utilized to determine mortgage interest rates. It had been the verbal consensus of industry leaders that this was an impossible task. No one index tracks mortgage rates that apply in all instances.

While we understand consumer groups' interest in creating rate "guarantees" that only fluctuate based on the movement of the cost of funds, one must understand that mortgage loans are not products that can be purchased off a shelf similar to purchasing a television from a store. Interest rates are complex risk assessments based upon underwriting of the consumer's ability to repay as well as the collateral which secures the mortgage loan. Interest rates are not merely based on an index; other factors may apply, such as warehouse line capacity, number of originations in the pipeline, product availability and others. NAMB cannot support this proposition as it will be nearly impossible with which to comply.

14. **As discussed in the preamble to the rule in Section III. C (5), if an observable index or other appropriate means of protecting borrowers from increases in lender compensation when the borrower floats in a guaranteed packaging approach is not practical, should HUD provide a packaging safe harbor only for mortgage brokers? Such a mortgage broker safe harbor would require disclosing the lender credit to the borrower in broker guaranteed packages. The theory for the safe harbor would be that any amounts in indirect fees could be credited to borrowers taking away any incentive for an increase in rates to increase compensation. Should this be offered in any event?**

Again, HUD singles out mortgage brokers in requesting responses to this question. As discussed above, earlier in this letter, NAMB does not support the characterization of the yield spread premium as a "lender payment to the borrower." This characterization is fraught with problems as described above. Further, it is not in keeping with the Statements of Policy 1999-1 and 2001-1. Thus, if disclosure of a yield spread premium as a "lender payment to the borrower" were the prerequisite to a safe harbor, NAMB could not support the safe harbor as the consequences would be too great to its industry.

15. **As proposed in section III. C (6), under the rule, mortgages with total fees or a rate covered by the Home Ownership and Equity Protection Act (HOEPA) would be subject to the new GFE disclosure requirements; however, HOEPA loans would not qualify for the guaranteed package safe harbor. Is this exclusion appropriate considering, on the one hand, that packaging promises borrowers a simpler way to shop and make transactions more transparent? On the other hand, the safe harbor could be provided for a loan that has very high rate and/or fees and may be predatory. The proposal also says that during the rulemaking other limitations may be established to exclude high cost and/or loans with predatory features from the packaging provisions. HUD invites comments on whether HOEPA loans, any other loans, or features of loans should be included or excluded from the safe harbor and why.**

As a general statement, exceptions should not be made for loans subject to HOEPA. The Truth in Lending Act has provided higher levels of protections for loans that meet the thresholds contained in HOEPA. By creating exceptions for special loans, these loans will continue to carry a stigma as they do today. Consistency among loan types will only benefit both consumers and industry. Providing different disclosure schemes for loans that are subprime, HOEPA loans, first lien mortgage loans, subordinate lien mortgage loans just leads to confusion for both consumers and industry and creates compliance difficulties.

Further, a HOEPA loan is not necessarily a "predatory" loan. Unfortunately, the words "HOEPA loan," "subprime loan," and "predatory loan" are incorrectly thought to be interchangeable. It seems that everyone's definition of what constitutes a "predatory" loan or an abusive loan practice differs. Some contend that prepayment penalties are a predatory practice as they lock consumers into loans; others contend that they are necessary loan features in order to ensure that a lender does not lose money on a loan due to "flipping." Identifying and defining predatory loans or features has been discussed among industry and consumers for years with no clear conclusions. Including any, with special protections, in the Proposed Rule would be extremely difficult and controversial. More study and analysis is necessary before HUD should take this step.

16. As proposed in Section III. C (3), the GMPA provides that the offer must be open to the borrower for at least 30 days from when the document is delivered or mailed to the borrower. Is this an appropriate minimum time period to ensure that the borrower has an adequate opportunity to shop?

NAMB supports allowing a consumer a certain period of time in order to shop for a mortgage loan. However, keeping guarantees of fees available to consumers for thirty (30) days or more presents several problems. Certain discounts capitalized on by originators may not be available for that length of time. As such, an originator will be forced to charge the higher fee and consumers will be disadvantaged by not having access to these lower fees. Further, unfortunately, in today's corporate environment, a great deal can happen to a company within thirty (30) days. For example, a title company, that gives all outward appearances to be in good corporate health, offers savings to originators who pass this savings through to their consumers, suddenly declares that it cannot honor its commitments. Under the Proposed Rule, an event like this, with thirty (30) day guarantees or tight tolerances in place, could destroy a small business. As such, NAMB has not supported the guarantee of third party fees (for this and other reasons) as well as maintaining the guaranteed fees availability for thirty (30) days.

Further, HUD's belief that the offer, guarantees included, can remain open for thirty (30) days, also lends support to the fallacy that mortgage loans are products that can be pulled from the shelf similar to televisions in an appliance store. These are unique products; maintaining the availability of these guarantees for thirty (30) days, will wreak havoc with lender's risk management.

Decreasing the amount of time a disclosure of fees is available to consumers does not prevent consumers from shopping for and comparing mortgage loans. Rather, a shorter period of time places some responsibility on the consumer to conduct this process in a timely manner. NAMB suggests seven (7) days availability for shopping.

17. As proposed in Section III. C (4), the rule currently provides that the Guaranteed Mortgage Package agreement must indicate that certain reports such as the appraisal, credit report, and pest inspection are available to the borrower upon the borrower's request. Also, packagers may decide to forego such reports or services (i.e. lender's title insurance) and must inform the borrower that such reports or services are not anticipated to be included in the package price. Are these adequate protections for the borrower? HUD is aware that other laws such as Regulation B (ECOA) provide certain rights to borrowers with respect to obtaining some of these reports. In order to qualify for the safe harbor HUD has created additional reporting requirements. Are these additional reporting requirements appropriate?

Respectfully, NAMB does not believe that all reports should be available to the consumer for the following reasons: (i) it may be against the law; (ii) the Proposed Rule disclosure does not provide the circumstances in which these reports must be disclosed; (iii) the reports are not prepared for the consumer's protection but for the lender's protection; and (iv) are superfluous in consideration of other federal disclosure requirements. First, for example, an originator might be in violation of the federal Fair Credit Reporting Act and their individual contracts with the credit resellers by providing copies of credit reports to the consumer unless the originator has taken an adverse action on the loan based on the credit report information.[93]

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[93] 15 U.S.C. § 1681e(c).

Second, the language in the Proposed Rule does not include any restrictions on when a report may be available to a consumer, based on federal or state law. For example, ECOA, which is implemented by the Federal Reserve Board, provides that a consumer may obtain a copy of their appraisal. An originator[94] may either routinely provide a copy of the appraisal or a notice informing the consumer that a copy of the appraisal is available upon request.[95] However, the consumer must notify the originator within 90 days after the originator notifies the consumer about the action taken on a credit application or the consumer withdraws its application.[96] Further, ECOA allows an originator to charge for the copying and mailing of a copy of the appraisal report.[97] An originator may also charge for the copy of the appraisal report if the consumer did not pay for the appraisal.[98] A disclosure, such as one contemplated in the Proposed Rule, will directly conflict with the provisions of ECOA and Regulation B, its implementing regulation. Consumers will be led to believe that they can obtain a copy of their appraisal at any time, regardless of whether the consumer paid for the appraisal. In addition, the sample disclosure provided under ECOA is quite clear and simple for the consumer. This Proposed Rule's disclosure of the availability of this report conflicts with the parameters available to consumer under ECOA and Regulation B.

Third, many of the reports, such as credit reports, pest inspections, appraisals and others, are not for the benefit of the consumer. Rather, these reports are for the benefit of the lender. The lender requests these reports to ascertain that the consumer is a sufficient credit risk or that the value of the house meets underwriting criteria and will adequately secure the loan obtained by the consumer. While we understand that these reports might provide the consumer with certain information, a better solution to this issue is to encourage all consumers to obtain an inspection on the property. At times, especially in today's market in certain places around the country, a consumer might forgo an inspection in connection with a purchase to create an incentive for a seller to accept their offer. In a refinancing transaction, a consumer might forgo an inspection because they feel that they "know their house."

Another example of this instance is where a lender obtains or does not obtain lender's title insurance on the secured property. New products become available every day for lenders to ensure that the consumer will hold good title to their property. Other lenders may find it a calculated risk to forgo lender's title insurance based upon the location of the property or for other reasons. Lender's title insurance is required only to protect the lender's risk that the consumer will not hold good title. A consumer is free to obtain owner's title insurance on any loan. NAMB does not find it appropriate to explicitly warn consumers that their loan does not have lender's title insurance as it does not protect the consumer.

Finally, as stated above, much of this information might be superfluous. For example, ECOA requires creditors to provide consumers with either a copy of their appraisal or a notice detailing how a consumer may obtain a copy of their appraisal. Thus, the information disclosed on the proposed disclosures under the Proposed Rule will be superfluous and redundant.

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[94] Credit unions are not required to comply with this requirement. 12 C.F.R. § 202.5a(b).
[95] 12 C.F.R. § 202.5a(a)(i).
[96] 12 C.F.R. § 202.5a(a)(ii).
[97] Regulation B Commentary § 202.5a. This is permissible unless it conflicts with state or other law. *Id.*
[98] *Id.*

18. Should additional consumer protections be established for packaging? For example, should additional qualifications be established for "packagers" to ensure that borrowers are protected against non-performance including the unavailability of a mortgage that could result in a borrower "losing" a house? For example, should there be a requirement that a packager must have sufficient financial resources to credibly back the guarantee? Is it necessary to require a lender signature on the GMPA to ensure that the borrower receives the loan at the time of settlement? How can the borrower's interests be protected without unduly burdening the process or unduly limiting the universe of packagers?

NAMB does not believe that packaging will benefit consumers or industry. As stated above, NAMB does not support packaging, as proposed by HUD, as it will disadvantage small business. Further, NAMB believes that this will not benefit consumers as it eliminates any Section 8 restrictions, such as the prohibition against upcharging of settlement costs. If small business is driven from the market due to packaging, larger entities will have no restrictions from engaging in these practices as they will have market share.

Further, requiring an entity to have "sufficient" financial resources to credibly back an offer amounts to requirements not unlike those a state requires for licensure. As stated above, 47 jurisdictions maintain some form of licensing, registration or notification requirement. These states have determined what standards are necessary for activity in their jurisdiction. If HUD were to impose such a requirement, it would seem to be creating barriers to entry that seem better handled by the state.

Further, NAMB does not support any instance in which a lender signature is required for a mortgage loan transaction to proceed. This creates an unlevel playing field for mortgage brokers. NAMB is concerned that some do not understand the part a mortgage broker plays in a transaction. In a mortgage broker transaction, if a mortgage lender fails to originate the mortgage loan, the consumer does not seek out the mortgage lender. Rather, the consumer holds the mortgage broker responsible for this transaction. Often, the mortgage lender, in a mortgage broker transaction, has no contact with the consumer. To a consumer, the mortgage broker is the originator. Thus, requiring a lender signature on the transaction places a consumer on an unlevel playing field with mortgage lenders and does not take into account a mortgage broker's role in the transaction.

NAMB believes that a consumer will be afforded additional protections under its proposed strengthening of the good faith estimate. The information provided to consumers will be firmer, and simpler to use for shopping purposes. It does not place extraordinarily undue burden on originators, placing them at risk to lose money with strict guarantees. NAMB believes its proposal will reduce the lure of engaging in bait and switch practices on the part of unscrupulous originators. Further, it attempts to level the playing field among originators, placing no one segment of the mortgage industry at a disadvantage. NAMB does not believe that packaging will accomplish these goals.

19. Consistent with the HUD-Fed Report, the rule proposes that certain charges, such as hazard insurance and reserves, are outside the package as other or optional costs. Is this the right approach or should these charges be disclosed as the minimum amounts required by the lender and required to be inside the package? Would the latter better serve the objective of establishing a single figure for the borrower to shop with?

As stated earlier, inclusion of third party settlement costs, over which the originator has little or no control, puts the originator at an economic disadvantage. If originators are to guarantee these costs, they run the risk of not covering the costs of originating a mortgage loan should an unforeseen event occur. Indeed, the fees in question, hazard insurance, reserves, taxes, mortgage insurance and per diem, should be carved out of the settlement costs and not subject to any kind of tolerance or guarantee. These fees are so dependent on different variables, such as when the loan closes, personal choice of the originator, that they cannot be held to any special tolerance.

For example, hazard insurance is typically a product that the consumer obtains of their own accord. Many states require that a consumer have the ability to choose their own insurers. Further, this amount, as cited in the HUD/Federal Reserve Board Joint Report, "depends upon consumers' choices unrelated to the credit transaction (such as the purchase of additional personal property or liability coverage)."[99] Thus, this amount should not be guaranteed or even placed within a tolerance.

NAMB's proposal provides two figures a consumer utilizes in shopping: (i) origination costs; and (ii) settlement costs. However, it carves these costs out for the above reasons. The form proposed by NAMB does estimate these costs and provides disclosure of them on the second page of the form.

20. The rule proposed in Section III.C (3), that under Guaranteed Mortgage Packaging, the HUD-1 will list the settlement services in the package but not the specific charges for each service. Certain third party charges are excluded from the calculation of the finance charge and the APR under TILA and HOEPA. Commenters are invited to express their views on whether the approach in the rule satisfies or whether alternative approaches to cost disclosures should be established to ensure consumer's rights under TILA and HOEPA are protected while facilitating packaging. More broadly, commenters are invited to provide their views on means of better coordinating RESPA and TILA disclosures.

NAMB does not support non-itemization of the costs included in the package. HUD inquires specifically whether the "listing" of fees satisfies the requirements under the Truth in Lending Act. The Proposed Rule provides that an originator can provide a consumer with a GMPA in lieu of a good faith estimate. Under the Truth in Lending Act, a creditor may provide a consumer with good faith estimate in lieu of an Itemization of Amount Financed.[100] The GMPA does not provide for an itemization of the costs associated with the mortgage loan, and under the Proposed Rule, the HUD-1 will mark the third party settlement services performed for the loan (but not the amounts) and will disclose on an Addendum the finance charges necessary to calculate the annual percentage rate.[101] It is unclear from the Proposed Rule whether the Addendum will include the actual amounts of the costs or just the names of the fees included

[99] "Joint Report to the Congress Concerning Reform to the Truth and Lending Act [sic] and the Real Estate Settlement Procedures Act," July 1998 at 24.
[100] 12 C.F.R. § 226.18(c), footnote 40.
[101] Proposed Rule, Fed. Reg. at 49,161.

in the finance charge. However, our reading of the Proposed Rule and the above question leads us to believe that the fees will be listed but not the amounts of the fees.

Based on this assumption, the consumer will be left with no avenue in which to determine that the annual percentage rate is accurate nor will the consumer be able to compare the costs included in the calculation of the annual percentage rate when shopping for a mortgage loan. Further, if an originator provides the Itemization of Amount Financed to consumers in addition to the GMPA, this might be confusing to consumers because not all fees associated with the mortgage loan are required to be included in the finance charge.[102] Will this diminish the value of the Truth in Lending annual percentage rate disclosure? Will this be a detriment of the consumer? We believe it will. We are concerned that HUD is unilaterally impacting a statute and implementing regulation over which it has no authority.

Under HOEPA, the definition of "points and fees" includes and excludes certain defined fees. As fees are only required to be listed on the GMPA and not enumerated, it provides no method to verify whether the loan meets the points and fees trigger under HOEPA based upon the fees charged. In other words, an unscrupulous lender may "alter" its list of fees charged to include fees that are excluded from the definition of "points and fees" to prevent the loan from falling under HOEPA.

Under NAMB's proposal, we continue to advance itemization of the costs involved in settlement of a mortgage loan. Not only does it provide information that mortgage brokers know from experience consumers will ask for, but it will maintain the value of the Truth in Lending annual percentage rate disclosure for consumers, as well as not create confusion for consumers. Further, unscrupulous lenders will not be able to circumvent the provisions of HOEPA by adjusting those fees contained in the calculation of "points and fees."

21. Commenters are asked to provide their views on how the rules should treat mortgage insurance? The rule proposes in Section III. C (3), that the guaranteed package would include any mortgage insurance premiums in the APR and up-front costs of mortgage insurance in the guaranteed package. "Other Required Costs" would include reserves for mortgage insurance premiums. However, because the packager will not have an appraisal at the time the GMPA is provided, the packager may not have firm information to provide a definite figure. Another possibility is to exclude mortgage insurance from the package but notify the borrower that mortgage insurance may be an "Other Required Costs" and present the borrower an estimate subject to a tolerance, if mortgage insurance is necessary. This approach would exclude a major charge from the package. HUD recognizes that there are state laws that prohibit rebates or any splitting of commissions for mortgage insurance. How, if at all, should this impact the decision to include mortgage insurance in packages of settlement services?

The concept of packaging relies on the premise that an originator can guarantee most third party costs and still remain competitive. Placing the obvious impact on small business in connection with the ability to compete in a packaging world aside, larger lenders are more able to absorb the losses stemming from an underestimation of the amount of mortgage insurance than small originators, such as mortgage brokers. For small businesses, incrementally, these amounts can ultimately drive an originator from the business as it is no longer profitable for them to originate mortgage loans. As such, a small originator might lean toward overestimation of these costs based on the fact that they cannot absorb losses as easily as the

[102] 12 C.F.R. § 226.4.

larger entities. This again renders small originators, such as mortgage brokers, less competitive than larger originators in the packaging regime.

Further, as one can imagine, many consumers tend to overinflate or underinflate the value of their home when seeking financing. While much of this is done innocently, it does not provide the originator with an accurate picture of the value of the property on which the originator must either estimate (within a tolerance) or guarantee the cost of mortgage insurance. Again, this will greatly impact small originators, such as mortgage brokers, who cannot absorb losses for underestimation of costs.

Mortgage insurance, and other third party fees that are also beyond the control of the originator, must be excluded from any guarantees.

22. To what extent, if any, do inconsistencies currently exist, or would they exist upon promulgation of the proposed rule between State laws and RESPA? Specifically, what types of State laws result in such inconsistencies and merit preemption? What, if any, provisions of the proposal should be revised to facilitate any necessary preemption?

RESPA provides the Secretary with certain preemption powers in connection with any conflicts of state law. Section 18 of the Act specifically allows that the Act does not preempt state laws, "except to the extent that those laws are inconsistent with any provision of this Act, and then only to the extent of the inconsistency."[103] RESPA authorizes the Secretary "to determine whether such inconsistencies exist."[104] Further, "the Secretary may not determine that any State law is inconsistent with any provision of this Act if the Secretary determines that such law gives greater protection to the consumer."[105] However, it also requires the Secretary to "consult with the appropriate federal agencies."[106] NAMB believes that the only method for achieving HUD's goals in implementing this proposed rule, is for HUD to preempt all state laws insofar as they conflict with aspects of the Proposed Rule. While an exhaustive review of all state laws and regulations, including the District of Columbia, is a time consuming venture and for which there has not been adequate time during this comment period, we have highlighted several areas of conflicts. Specific state conflicts will be enumerated on Exhibit C to this letter.

Certain states require that, in connection with a mortgage loan, a consumer be allowed to choose its own title attorney or title insurance provider. As this fee is part of the package and thus guaranteed, it is uncertain how a packager can guarantee this costs when the consumer may choose its own title attorney or title insurance provider. This creates a conflict for packagers of settlement costs. Similar arguments apply to attorney's fees, as many states allow a consumer to choose its own attorney, as well as hazard insurance.

Certain states require the provision of the itemization of fees. In HUD's Proposed Rule, under the packaging scheme, these fees would be required to be listed but not itemized. For example, in California, a mortgage broker must provide the consumer with an itemization of certain settlement costs.[107] In New York, a mortgage broker must provide the consumer, pre-application, with a disclosure of certain fees, such as an application fee, appraisal fee, and credit report fee.[108] In Texas, a mortgage broker must

[103] 12 U.S.C. § 2616.
[104] *Id.*
[105] *Id.*
[106] *Id.*
[107] Cal. Bus. & Prof. Code § 10241.
[108] N.Y. Comp. Code R. & Regs. tit. 3, § 38.3.

disclose application the application fee, processing fee, appraisal fee, credit report fee, automated underwriting fee and other fees that will be charged in connection with the loan.[109] This will conflict with the requirements for the packaging world in the Proposed Rule, as enumeration of the costs of these fees is not required.

Certain states will prevent a mortgage broker from providing a loan commitment. In New York, a mortgage broker is prohibited from making a loan commitment to a consumer.[110] Thus, mortgage brokers will be unable to compete in the packaging world in the State of New York.

A major conflict occurs in connection with licensing issues for settlement service providers who wish to provide packages. As the Proposed Rule requires that a package of settlement services must be delivered with a mortgage loan, some settlement service providers will need to obtain a mortgage broker license. Most states require that mortgage brokers obtain a license, register or provide notification for the arranging of a mortgage loan. Some entities will be faced with these additional licensing requirements.

There are some very real conflicts that occur between the Proposed Rule and state law. Without federal preemption of these state laws, the packaging process will not provide the benefit sought in many states. NAMB's proposal, on the other hand, can eliminate many of the conflicts described above. For example, costs will continued to be itemized in NAMB's proposal.

23. The rule proposes that the GFE and the GMPA be given subject to appraisal and underwriting. How should the final rule address the matter of loan rejection or threatened rejection as a means of allowing the originator to change the GFE or GMPA to simply earn a higher profit?

This is a difficult issue to address and requires that a balance be sought. NAMB agrees that certain unscrupulous members of the industry will utilize this caveat as a tool to increase profitability. But in keeping with the maxim "don't throw the baby out with the bathwater," taking away exceptions leads to one conclusion – an increase in the amount of costs to eliminate loss to industry. HUD must understand that any losses sustained by industry will ultimately be passed through to consumers in the form of higher costs for the origination of a mortgage loan. Further, there are legitimate reasons for maintaining an exception: many fees are dependent on loan to value ratios, loan amount and term of the mortgage loan. Further, we believe that HUD would find it difficult to enforce this practice under RESPA.

As such, NAMB's proposal seems to provide added protection for consumers while providing a manageable process for mortgage originators with a limitation on unnecessary losses – redisclosure with enough time for consumers to accept or reject the costs before settlement. The proposal includes tight tolerances for the final disclosure of costs in order to avoid any "bait and switch" prior to settlement on the part of the originator yet provides the originator with enough information on the property and the consumer's credit to make an educated disclosure of the costs for settlement.

Further, we encourage HUD to work with the Federal Reserve Board in seeking changes to the adverse action notices and counteroffer notices. Changes can be made to these forms which provide hard and documentable reasons for a consumer not qualifying for a certain loan program or an increase in loan amount.

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[109] 7 Tex. Admin. Code Part 80 (sample disclosure form).
[110] N.Y. Comp. Code R. & Regs. tit. 3, § 38.3.

24. To what extent, if any should direct loan programs such as those provided by the Rural Housing Service of the Department of Agriculture be treated differently under the new regulatory requirements proposed by this rule?

NAMB firmly believes in leveling the playing field for all originators as well as for all consumers. Consistency in disclosures provides the consumer with a comfort level in understanding their transaction and its origination. Congress and other agencies are free to dictate other protections for consumers or requirements for originators who originate these loans, but there should be continuity among the disclosures that are provided to consumers regardless of the type of loan being originated.

25. As proposed, the GFE and GMPA currently contain sections for loan originators and packagers to indicate the specific loan terms for adjustable rate mortgages, prepayment penalties, and balloon payments. Are these appropriate loan terms to include on these forms, and what, if any, other mortgage terms or conditions should be listed on the forms?

NAMB supports the inclusion of these loan terms and has included them in our proposal for improving the good faith estimate. These loan terms are often disclosed in other disclosures, such as the Truth in Lending annual percentage rate disclosure[111] and certain state law disclosures. However, NAMB supports their redisclosure as potentially helpful to the consumer to avoid any abusive practices of "hiding" these loan terms. NAMB supports this notwithstanding any duplicative disclosure to consumer or additional regulatory burden it may place on originators. Further, we have included disclosing whether the loan is assumable in our proposal.

26. What are the arguments for or against limiting the proposed rule to purchase money, first and second lien, and refinancing loans as opposed to offering it to home equity, reverse mortgage and other transactions? Should there be any additional requirements for so called B, C, and D loans?

One of the greatest regulatory burdens to industry is maintaining different disclosure schemes and requirements for different mortgage loans. Of course, different disclosures are inherently necessary for different loan products, such as reverse mortgage loans and home equity lines of credit. NAMB supports the maintenance of status quo as opposed to expanding RESPA's early disclosure requirements beyond its current scope. Further, NAMB supports utilizing the same disclosure scheme regardless of the type of transaction.

For example, HUD has exempted home equity lines of credit from the good faith estimate disclosure requirement under Section 3500.7(f) (please note that is unclear whether the GMPA would also be considered exempt based upon this exemption). The Federal Reserve Board, under Section 226.5b(d)(7) of Regulation Z, requires creditors to provide "an itemization of any fees imposed by the creditor to open, use, or maintain the plan, stated as a dollar amount or percentage, and when such fees are payable." Thus, settlement costs are disclosed to consumers under a separate federal law.

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[111] Regulation Z requires the disclosure, in its annual percentage rate disclosure, whether the loan has a prepayment penalty, whether the loan is assumable, whether the loan is an adjustable rate mortgage loan, and other information. 12 C.F.R. § 226.18. Further, Regulation Z requires that an adjustable rate loan program disclosure and a "Consumer Handbook on Adjustable Rate Mortgages" be provided to a consumer for every adjustable rate loan program in which the consumer expresses an interest. 12 C.F.R. § 226.19(2).

Creating different regulatory schemes for different loan types can create confusion for consumers as well as create room for error on the part of industry. The definition of a subprime loan differs based on underwriting criteria. Each lender may have a different definition of what constitutes a subprime loan. Further additional protections are available for certain subprime loans under HOEPA.

27. As proposed, the Guaranteed Mortgage Package includes one fee for settlement services required to complete a mortgage loan. The fee for the package will include loan origination fees, typically referred to as "points." As points are generally deductible under IRS rules, comments are invited as to how to determine which portion of the package prices should be deemed to constitute points.

A simple answer to this question is to require the disclosure of points to consumers. This is very valuable tax tool that is utilized by consumers. NAMB maintains the disclosure of points as a line item, which is clearly identifiable, on its proposal. Further, it should continue to be disclosed on the HUD-1.

28. To what extent do the proposed changes to the definition of application in Section III. B (2) a., and requirements for delivery of the GFE impact other federal disclosure requirements, such as those mandated by the Truth in Lending Act? How can the disclosure objectives of the proposed rule be harmonized with such other disclosure requirements?

NAMB supports the maintenance of status quo in connection with the definition of what constitutes an "application." While NAMB understands that HUD's Proposed Rule codifies informal advice set forth by HUD, NAMB believes that enforcement of this provision will be difficult. States who maintain loan logs will be rife with loans that are never originated and loan officers might encounter difficulty with ascertaining whether an "application" was truly created. Further, as there are different definitions of what constitutes an "application" among the different federal and state laws, it creates a compliance minefield for originators.

29. The proposed rule in Section III. B (2) c., would require a loan originator capable of offering an alternative loan product to provide a prospective borrower, upon the borrower's request, with a new GFE if, after full underwriting, the borrower does not qualify for the loan identified on the original GFE. Is this approach appropriate? What other options should be considered where borrowers do not qualify for the loan product initially sought?

This approach is in keeping with current requirements under ECOA and RESPA. Adverse action notices or counteroffer notices are required to be provided when a borrower does not qualify for a loan product or program but does qualify for another loan product or program.[112] These notices could be amended to provide descriptive and documentable reasons for the adverse action or counteroffer. We encourage HUD to work with the Federal Reserve Board to amend these notices to provide the maximum benefit to consumers. This will benefit industry as hard and fast rules could be maintained for the documenting of these actions and the reasons surrounding them.

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[112] 12 C.F.R. § 202.9(a).

30. The proposed rule in Section III. B (2) c., would require loan originators to provide qualified borrowers with an amended GFE, identifying any changes in costs associated with changes in the interest rate, where the borrower elects not to lock-in the interest rate quoted on the original GFE at the time it is provided. Is this an appropriate requirement? What alternatives, if any, should HUD consider?

NAMB does not support redisclosure of changes in cost each time the interest rate changes if the consumer elects to float their interest rate. NAMB believes that the redisclosure requirements it proposes will be simpler to effect, as well as provide less paperwork for the consumer. Redisclosure is required when the loan program changes, the property changes or does not qualify, the consumer chooses a different pricing option, the consumer is not eligible for the loan, or the loan amount changes. Further, redisclosure is also required fifteen (15) days prior to settlement if the settlement costs have increased. As contemplated in this question, if this disclosure were provided for each instance of a fluctuation in the interest rate, an originator could never make more than one mortgage loan at a time for all of the disclosing required.

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We thank HUD for the opportunity to comment on the Proposed Rule. If you have any questions about the forgoing discussion, please do not hesitate to contact NAMB's Legislative Committee Chair Neill Fendly at (480) 905-8882 or NAMB's Director of Legislative and Regulatory Affairs Stephanie Shaw at (703) 610-0205.

Sincerely,

Armand W. Cosenza, Jr., CRMS
President

UNIFORM MORTGAGE COSTS DISCLOSURE

Please take this disclosure with you to settlement to compare costs.

We agree to perform or provide services, goods or facilities to assist you in the origination of a mortgage loan. The services, goods or facilities may be performed or provided for your direct benefit, or some of them may benefit you only indirectly, in that they are performed on behalf of third parties (e.g., wholesale lenders or secondary market investors) but are necessary to the objective of obtaining the mortgage loan you desire. While we seek to assist you in meeting your financial needs, we cannot guarantee the lowest price or best terms available in the market. We, as with all originators, may not offer all the products that are available in the marketplace.

The information provided below reflects our disclosure of the charges you will incur at the settlement of your loan. The "Origination Costs" are fees charged by your originator or an investor for providing a mortgage loan. "Settlement Costs" are fees for third party services that are required for the mortgage loan to close. These "Total Costs" are itemized for you in the grid below.

The following disclosure is valid for _____ days (7 days or greater) from the date this form is delivered to and signed by the borrower. This disclosure is dependent upon the borrower qualifying for this mortgage based on their credit rating, appraisal, and other appropriate criteria.

Summary of Loan Terms:
Property Address: ______________________________
This loan will be a _____ purchase _______refinance. This loan will be a ______ first mortgage _____second mortgage.
Loan Program: ______________________________Loan Term: ____________ Mortgage Loan Amount: ____________________
(See appropriate disclosure form)

%

Interest Rate ______ Initials

This is the interest rate for [today] for the loan you have selected. We will lock this rate for you for the following time period of _____ days. This interest rate lock will expire _______. I understand to obtain this interest rate loan. I may be required to pay a lock fee which is NOT INCLUDED in the costs disclosed on this form. If you choose not to lock your interest rate today, your interest rate may increase or decrease before settlement without notification.

_______**I want to lock my interest rate.** ______________ ______________
By signing above, you have agreed that this is the interest rate you will pay for this loan provided you qualify, regardless of market conditions. For this interest rate lock, you agree to pay $__________.

______ **I choose not to lock my interest rate. I understand that my interest rate may increase or decrease before settlement without prior notification.** ______________ ______________

$

Origination Costs ______ Initials

This is the total amount of costs being charged as origination costs. These costs are itemized below. These costs will not increase unless you are not eligible for this loan program, your property changes or does not qualify, you choose a different loan program, you choose a different pricing option, or your loan amount changes. This figure does not include any settlement costs that are paid to a third party.

$

Settlement Costs ______ Initials

This is the total amount of costs you will incur for the settlement of this loan. These costs are itemized below. As these costs are beyond the control of the originator, they are not guaranteed. However, if these fees change from initial disclosure, the originator is required to redisclose to you at a minimum of fifteen (15) days prior to settlement. Upon final disclosure, this amount cannot increase beyond 10% of the amount of the total amount of fees at settlement. You may waive the 15-day redisclosure requirement under certain conditions.

This figure does not include the following four costs: any escrows set up for taxes, any escrows set up for homeowners insurance, any escrows set up for mortgage insurance, and any per diem interest. Please see page 2 of this disclosure for an estimation of your hazard insurance, mortgage insurance, taxes, escrow amounts, and per diem interest.

$

Monthly Payment ______ Initials

This is your monthly payment based on the above loan amount and the above interest rate. This payment **DOES** include the following:

_______ Principal.
_______ Interest.
_______ Hazard insurance.
_______ Real estate taxes.
_______ Mortgage insurance.

After reading through the above information, please initial to the right of each box to show your acknowledgement and acceptance of the above data. Also, you need to indicate your preference by signing either the float or lock option in the "Interest Rate" section.

These estimates are provided pursuant to the Real Estate Settlement Procedures Act of 1974, as amended (RESPA). Additional information can be found in the HUD Special Information Booklet, which is to be provided to you by your mortgage broker or lender, if your application is to purchase residential real property and the lender will take a first lien on the property. The undersigned acknowledges receipt of the booklet "Settlement Costs", and if applicable the Consumer Handbook on ARM mortgages. The undersigned also acknowledges that I (we) have read both pages of this disclosure and that I (we) fully understand its terms. Further, by signing below, the undersigned authorize the originator to ______ order an appraisal, a credit report and continue the origination process___ draw documents in order to proceed to settlement.

______________________________ ______________________________
Borrower Date Co-Borrower Date

Itemization of Total Costs

Origination Costs		Settlement Costs	
801 Loan Origination Fee		803 Appraisal Fee	
802 Loan Discount		804 Credit Report	
808 Mortgage Broker Fee		805 Lender's Inspection	
810 Processing Fee		806 Flood Zone Certification Fee	
811 Underwriting Fee		809 Tax Related Service Fee	
812 Wire Transfer Fee		1101 Closing or Escrow Fee	
		1105 Document Preparation Fee	
		1106 Notary Fees	
		1107 Attorney Fees	
		1108 Title Insurance	
		1201 Recording Fees	
		1202 City/County Tax/Stamps	
		1203 State Tax/Stamps	
		1302 Pest Inspection	
		1303 Courier Fee	

Additional Costs

Certain costs are not included in the above estimates as they are based upon personal choice on your part or are dependent upon when closing will be held. These amounts are estimated below based upon a closing date of ________:

Per Diem Interest ___ days at $___ per day = ________
Hazard Insurance for ___ months ________ Amount to be Escrowed Each Month ________
Taxes for ___ months ________ Amount to be Escrowed Each Month ________
Mortgage Insurance for ___ months ________ Amount to be Escrowed Each Month ________

The total estimated amount of your monthly payment, based upon your loan program and amounts to be escrowed, is ________.

Interest Rate and Settlement Costs Options

1. Cash Payment at Settlement: You may pay all or part of your required settlement costs at settlement using your available funds.
2. Borrowing Additional Funds to Pay Settlement Costs: You may be able to pay all or part of your settlement costs by borrowing the needed funds as part of your mortgage loan principal. If you choose this option, your monthly payments will increase. This may not be available on a purchase-money loan.
3. Pay Settlement Costs Through a Higher Interest Rate: You may be able to lower your settlement costs in exchange for paying a higher interest rate on your mortgage loan. This higher interest rate will increase your monthly payments.
4. You May Lower Your Interest Rate: You may be able to lower the interest rate on your loan by paying additional funds at closing, commonly referred to as "discount points." The reduced interest rate will lower your monthly payments.

The following table provides a generic example of how higher and lower interest rates affect your loan and loan payments.

	GFE Terms You Selected	Higher Interest Rate	Lower Interest Rate
New Loan Balance	$100,000	$100,000	$100,000
Interest Rate	7.00%	7.25%	6.75%
Monthly Principal & Interest & PMI (if required)	$700.30	$717.18	$683.60
Change in Cash to Close from GFE Terms You Selected		$1,000 less	$1,000 more
Change in Monthly P&I from GFE Terms You Selected		$16.88 more	$16.70 less

$

Initials

Compensation For Goods, Facilities And Services For Your Loan

An originator may be compensated by an investor for goods, facilities or services provided to you or to the investor. This will result in a higher interest rate for this loan. If you would rather pay less cash up front, you may be able to pay some or all of the originator's compensation indirectly through a higher interest rate. If you would rather have a lower interest rate, you may pay higher up-front points and fees. This amount will not exceed the amount disclosed to the left of this description.

If the originator is acting as a lender in this transaction, the originator may receive additional compensation when it sells the loan for the value of the servicing rights or the value of the interest rate or a combination of both. This amount is not required to be disclosed.

ADDITIONAL LOAN TERMS

- ☐ This mortgage IS subject to a prepayment penalty.
- ☐ This mortgage IS NOT subject to a prepayment penalty.
- ☐ This mortgage HAS a balloon payment of ________, which will be due at the conclusion of the loan term. We may or may not refinance this mortgage.
- ☐ This mortgage DOES NOT HAVE a balloon payment.
- ☐ This mortgage IS assumable.
- ☐ This mortgage IS NOT assumable.

Adjustable Rate Mortgage (ARM) Loans

___This is an Adjustable Rate Mortgage (ARM) Loan. Your interest rate may increase or decrease depending on the market. THAT MEANS THAT YOUR MONTHLY PAYMENT MAY INCREASE OR DECREASE. Please refer to the ________ loan program disclosure provided to you.

Details of Transaction

a. Purchase Price	
b. Refinance (debts to be paid off)	
c. Estimated Prepaid items	
d. Estimated Closing Costs	
e. PMI, MIP, Funding Fee	
Total costs a-e	
- Subordinate Financing	
- Costs paid by seller	
- Other credits	
- Loan amount	
Cash from/to borrower	

You will need to bring approximately $________ with you to settlement. This amount may change. This form must be signed and returned within seven (7) days of receipt.

National Association of Mortgage Brokers

<u>**Exhibit B**</u>

Discrepancies in HUD's Economic Analysis and Initial Regulatory Flexibility Analysis[1]

1. On page 22 HUD states that currently, $7.5 billion of YSP payments "is not passed through to borrowers." Under this proposal, HUD assumes that consumers will recapture half of that, or $3.75 billion. The mandate requires a dollar for dollar offset, meaning that consumers should get all $7.5 billion. Where does the other $3.75 billion go?

2. On page 22, HUD states that origination fees are estimated at $15 billion. HUD asserts that the mandate will improve a consumer's ability to shop and therefore capture five percent ($.75 billion). Why wouldn't a broker try to charge more in origination fees if HUD takes away the ability to charge a yield spread premium? In other words, the analysis is static. A small businessman is not just going to voluntarily cut his rates by half – which is what the HUD model assumes. Most small businesses do not have a 50 percent profit margin.

By not producing a more accurate and dynamic model, HUD is overstating the benefits of this proposal and understating the devastating impact on small business who provides high quality service and expertise.

3. The Proposed Rule will allegedly improve a customer's ability to shop and actually facilitate shopping. If this proposal achieves that goal – and it remains unclear at this time – then a customer could go to ABC bank get the GFE and then get in his/her car and drive to Broker X and compare GFE's.

While the ability to shop may be a desired outcome of public policy, it is difficult to accept the notion that increased shopping saves consumers $826 million. The physical act of shopping is not a costless exercise – and, more to the point of HUD's estimate, it does not *save* money. That is, no one pays a consumer for shopping. However, HUD's Economic Analysis ignores this transaction cost and arbitrarily asserts a savings.[2] This overstates the benefits of this proposal.

This is another example of how the static and questionable analysis is fundamentally flawed. As a result, HUD's Economic Analysis provides no basis to understand the real burden of the proposal.

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[1] "Economic Analysis and Initial Regulatory Flexibility Analysis for RESPA Proposed Rule to Simplify and Improve the Process of Obtaining Mortgages to Reduce Settlement Costs to Consumers," U.S. Department of Housing and Urban Development, Office of Policy Development and Research, July 2002.
[2] "Economic Analysis," p. 54.

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4. On page 54, HUD states that originators and third party settlement service providers will save time (and $850 million) by reducing the amount of time spent with a borrower. While this may be partially true, HUD does not account for the increased foot traffic and comparison shopping made possible by the new rule. An originator will spend more time answering people's questions that are "shopping." It is quite likely that originators will even be walking these shoppers through the new disclosures. This time and resources is not accounted for in HUD's analysis.

Again, HUD overstates the benefits with static analysis.

5. The last example is how HUD does not understand the marketplace and ends up creating an unlevel playing field for small business.

On page 30 HUD asserts that, "All broker income must be derived from direct fees while lenders who originate may continue to supplement their direct fees with yield spread premiums that continue to be unreported to borrowers. This may give lenders a competitive advantage over brokers." HUD goes on to say on page 32 that "A potential problem comes where a shopper is not knowledgeable. A lender trying to convince a borrower to take his loan instead of the broker's might focus the borrower's attention on the reported origination fee of the two charges…".

That is the point. Of course the lender is going to try to, as HUD says, "convince the borrower to take his loan." That is how the market works. The lender is not an unbiased party in this transaction. He is a competitor and will always try to convince the borrower to take his loan. This is why the current disclosure does not work in its current form – it creates an unlevel playing field.

NAMB
National Association of Mortgage Brokers

Exhibit C

State Law Conflicts

NAMB has performed an initial review and identified several areas in which state laws conflict with HUD's Proposed Rule. NAMB did not perform an exhaustive review of state laws; this would be a rather time consuming effort. Further, we have limited our research to first lien mortgage loan laws and requirements.

Certain Settlement Services Must Be Chosen By the Consumer:

Certain states require that, in connection with a mortgage loan, a consumer be allowed to choose its own title attorney or title insurance provider. As this fee is part of the package and thus guaranteed, it is uncertain how a packager can guarantee this cost when the consumer may choose its own title attorney or title insurance provider. This creates a conflict for packagers of settlement costs. Similar arguments apply to attorney's fees and hazard insurance, as many states allow a consumer to choose its own attorney and hazard insurance.

States in which a consumer must be provided the opportunity to choose its own title attorney or title insurance provider include, but are not limited to: Illinois (815 ILCS 205/244), Maine (Me. Rev. Stat. Ann. tit. 9-B, § 241.4), Maryland (Md. Code Ann., Com. Law II § 12-119(b)(2)), Rhode Island (R.I. Gen. Laws § 19-9-5), Vermont (Vt. Stat. Ann. tit. 9, § 42(b)), Texas (Tex. Ins. Code Ann.§ 342.404(c)).

States in which a consumer must be provided the opportunity to choose its own insurance provider include, but are not limited to: Alabama (Ala. Code § 5-19-20), Alaska (Alaska Stat. § 21.36.165), Arizona (Ariz. Rev. Stat. Ann. § 20-452.01), California (Cal. Ins. Code § 770), Hawaii (Haw. Rev. Stat. § 431:13-104(a)), Idaho (Idaho Code § 41-1310), Indiana (Ind. Code § 27-4-1-4(9)), Iowa (Iowa Code § 507B.5.1.a), Kentucky (Ky. Rev. Stat. Ann. § 304.12-150), Louisiana (La. Rev. Stat. Ann. § 22:1214(9)), Maine (Me. Rev. Stat. Ann. tit. 24-A, § 2169), Maryland (Md. Code Ann., Com. Law § 12-410(f)), Massachusetts (Mass. Gen. L. ch. 175, § 193E), Minnesota (Minn. Stat. § 72A.31), Montana (Mont. Code Ann. § 33-18-501), Nebraska (Neb. Rev. Stat. § 44-1526(a)), Nevada (Nev. Rev. Stat. § 686A.200), New Hampshire (N.H. Rev. Stat. Ann. § 417:4(XVI)(a)), New Mexico (N.M. Stat. Ann. § 59A-16-14), New York (N.Y. Comp. Codes R. & Regs. tit. 3, § 38.9), North Dakota (N.D. Cent. Code § 26.1-04-04.1), Ohio (Ohio Rev. Code Ann. § 3933.04), Oregon (Or. Rev. Stat. § 746.180), Tennessee (Tenn. Code Ann. § 56-8-106(a)(1)), Utah (Utah Code Ann. § 31A-23-302(5)), Vermont (Vt. Stat. Ann. tit. 9, § 42(b)), Virginia (Va. Code Ann. § 6.1-330.70), Washington (Wash. Rev. Code § 48.30.260(3a) and (3f)), Wisconsin (Wis. Stat. § 134.10(1)), and Wyoming (Wyo. Stat. § 26-13-118).

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States in which a consumer must be provided the opportunity to choose its own attorney include, bust are not limited to: Connecticut (Conn. Gen. Stat. § 49-6d), Maryland (Md. Code Ann., Com. Law II § 12-119(b)(2)), New Jersey (N.J. Rev. Stat § 46:10A-6), South Carolina (S.C. Code Ann. § 37-10-102), Virginia (Va. Code § 6.1-330.70), and Wisconsin (Wis. Stat. § 708.03).

Itemization is Required Under State Law at Application:

Certain states require the provision of the itemization of fees early in the origination process. In HUD's Proposed Rule, under the packaging scheme, fees would be required to be listed but not itemized early in the process. For example, in New York, a mortgage broker must provide the consumer, pre-application, with a disclosure of certain fees, such as an application fee, appraisal fee, and credit report fee.[1] This will conflict with the requirements for the packaging world in the Proposed Rule, as enumeration of the costs of these fees is not required at this stage.

States in which a mortgage broker must itemize certain fees at application include, but are not limited to: Arizona (Ariz. Rev. Stat. § 6-906.C), California (Cal. Bus. & Prof. Code § 10241), New York (N.Y. Comp. Codes R. & Regs. tit. 3, § 38.3), and Texas (7 Tex. Admin. Code Part 80).

Further, in certain states, fees must be disclosed early in order to collect them at closing. As neither the enhanced good faith estimate or the guaranteed mortgage package under HUD's Proposed Rule provides for this early itemization, this will prove difficult for originators to collect these fees at closing. Duplicate disclosures will be provided, complicating the structure HUD strives for. These states include, but are not limited to: Massachusetts (Mass. Gen. Law ch. 183, § 63), and New Hampshire (N.H. Rev. Stat. Ann. § 397-A:16(I)).

States in Which Certain Fees are Prohibited:

Certain fees are prohibited in certain states. For example, in Maryland, a lender's inspection fee can not be charged, except under certain circumstances.[2] In several other states, a mortgage broker may only collect certain fees at application. The Proposed Rule would permit the collection of a nominal fee under both the enhanced good faith estimate and the guaranteed mortgage package agreement. However, this is not a fee that is permissible in these states. Thus, a conflict would exist in connection with the charging of this nominal fee in certain states.

States in which fees may be charged at application which do not constitute a "nominal fee" as described in the Proposed Rule include, but are not limited to: Arizona (Ariz. Rev. Stat. Ann. § 6-906.C), Florida (Fla. Stat. Ch. 494.0042(3)), Idaho (Idaho Code § 26-3113), and New York (N.Y. Comp. Codes R. & Regs. tit. § 38.3(a)(2)(iv)).

Further, most states, including Delaware and Michigan, require that all fees charged be reasonable and necessary fees, and in many instances, actual costs. Under packaging, there will be no manner for state regulators nor consumers to determine whether the fees charged to them are reasonable in keeping with state law.

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[1] N.Y. Comp. Codes R. & Regs. tit.3, § 38(a)(1)(v).
[2] Md. Code Ann., Com. Law § 12-121(b).

States in Which a Mortgage Broker Cannot Offer a Commitment:

Certain states will prevent a mortgage broker from providing a loan commitment. In New York, a mortgage broker is prohibited from making a loan commitment to a consumer. [3] Thus, mortgage brokers will be unable to compete in the packaging world in the State of New York.

Packaging will Require Many Settlement Service Providers, and Others, who Participate in Packaging to Be Licensed as a Mortgage Broker:

A conflict occurs in connection with licensing issues for settlement service providers who wish to provide packages. As the Proposed Rule requires that a package of settlement services must be delivered with a mortgage loan, some settlement service providers will need to obtain a mortgage broker license to comply with this requirement. Most states require that mortgage brokers obtain a license, register or provide notification in order to act as a mortgage broker. Some entities will be faced with these additional licensing requirements. Currently, 46 states and the District of Columbia maintain licensing, registration or notification requirements for mortgage brokers. These requirements often include exemptions for certain entities, such as insurance agents or realtors (if the realtor does not engage in more than a certain number of transactions a year). However, the number of licensees, registrants or those providing notification will likely dramatically increase if the Proposed Rule is finalized.

Referral Fees Prohibited:

In several states,[4] a realtor cannot collect a fee for performing real estate services as well as collect a fee for acting as a mortgage broker in the same capacity. However, in HUD's proposed packaging world, the lines between a realtor and a mortgage broker will blur if the realtor participates in packaging. It will be difficult for consumers to understand, if HUD's Proposed Rule is finalized, what fees are charged for what activity. Further, in these states, a realtor will likely not engage in packaging as it will not be profitable.

Further, in certain states, it is illegal for "kickbacks" to be provided in connection with the sale of title insurance. For example, Virginia prohibits the payment of "kickbacks" in connection with title insurance.[5] This will be in direct contravention with HUD's Proposed Rule, if finalized.

[3] N.Y. Comp. Codes R. & Regs. tit. 3, § 38.3(a)(1)(i).
[4] Minnesota, Virginia and Connecticut are included in these states.
[5] Va. Rev. Stat. § 38.2-4614.

Attachment 3

SBA

Office of Advocacy

October 28, 2002

Richard A. Hauser, Esquire
General Counsel
Office of the General Counsel
Department of Housing and Urban Development
451 Seventh Street, SW
Washington, DC 20410-0500

Re: Department of Housing and Urban Development: Real Estate Settlement Procedures Act (RESPA); Simplifying and Improving the Process for Obtaining Mortgages to Reduce Settlement Costs to Consumers; Proposed Rule; Docket Number: FR-4727-P-01

Dear Mr. Hauser:

As part of its statutory duty to monitor and report on an agency's compliance with the Regulatory Flexibility Act of 1980 ("RFA"), as amended by the Small Business Regulatory Enforcement Fairness Act of 1996 ("SBREFA"),**(1)** the Office of Advocacy of the U.S. Small Business Administration ("Advocacy")**(2)** reviewed the Department of Housing and Urban Development's ("HUD") compliance with the RFA's requirements for the above-referenced Notice of Proposed Rulemaking ("NPRM").**(3)**

On July 29, 2002, the Department of Housing and Urban Development (HUD) published a proposed rule on the Real Estate Settlement Procedures Act (RESPA) in the *Federal Register*, Vol. 67, No.145, p. on page 49134. The purpose of the proposal is to simplify and improve the process of obtaining home mortgages and reduce settlement costs to consumers. The proposal addresses the issue of lender payments to mortgage brokers by changing the way that payments in brokered transactions are recorded and reported to consumers. It requires a Good Faith Estimate (GFE) settlement disclosure and allows for packaging of settlement services and mortgages.

After reviewing the NPRM and discussing it with affected small businesses,**(4)** Advocacy would like to encourage HUD to issue a revised initial regulatory flexibility analysis (IRFA) that takes into consideration the comments of affected small entities and develops regulatory alternatives to achieve HUD's objectives while minimizing the impact on small businesses.

RFA Requirements for a NPRM

The RFA requires agencies to consider the economic impact that a proposed rulemaking will have on small entities. Unless the head of the agency certifies that the proposed rule will not have a significant economic impact on a substantial number of small entities, the agency is required to prepare an IRFA. The IRFA must include: (1) a description of the impact of the proposed rule on small entities; (2) the reasons the action is being considered; (3) a succinct statement of the objectives of, and legal basis for the proposal; (4) the estimated number and types of small entities to which the proposed rule will apply; (5) the projected reporting, recordkeeping, and other compliance requirements, including an estimate of the small entities subject to the requirements and the professional skills necessary to comply; (6) all relevant Federal rules which may duplicate, overlap, or conflict with the proposed rule; and (7) all significant alternatives that accomplish the stated objectives of the applicable statues and minimize any significant economic impact of the proposed rule on small entities.**(5)** In preparing its IRFA, an agency may provide either a quantifiable or numerical description of the effects of a proposed rule or alternatives to the proposed rule, or more general descriptive statements if quantification is not practicable or reliable.**(6)**

HUD's Compliance with the RFA

Pursuant to the RFA, HUD prepared an IRFA in conjunction with its Economic Analysis prepared under Executive Order 12866.**(7)** Section 605 of the RFA expressly permits agencies to perform an IRFA in conjunction with other analyses provided the analysis meets the requirement of the RFA. For the reasons stated below, Advocacy is of the opinion that further economic analysis prepared by HUD, in a revised IRFA, would improve the Final Rule.

Defining Small Businesses Affected by the RESPA Proposal

Section 601 of the RFA requires an agency to use the definition of small business contained in the U.S. Small Business Administration's ("SBA") small business size standards regulations,**(8)** promulgated by the SBA under the Small Business Act.**(9)** Below is a table of the SBA's definition of small business for the industries in which small businesses have contacted the Office of Advocacy to raise concerns regarding the impacts of this rule.**(10)**

NAICS Code	**Industry Description**	**SBA Size Standard (revenues <=) in $ millions**
531210	Mortgage Brokers (Real Estate Agents and Brokers)	6
522292	Real Estate Credit	6
541191	Title Abstract and Settlement Offices	6
531320	Offices of Real Estate Appraisers	1.5
561710	Pest Inspectors - Exterminators	6

The proposed rule will affect mortgage brokers, mortgage lenders, realtors, appraisers, pest inspectors, and settlement service providers. Although HUD acknowledged that the majority of the businesses in the industries affected by the rule are small businesses, its economic analysis would improve by a revised IRFA that clearly defines the impact on those small entities.

HUD's analysis included the overall cost of compliance for the proposal in its analysis. A revised IRFA would allow for HUD to compute the compliance cost per small entity. This would enable HUD to identify and analyze significant regulatory alternatives to minimize the potential burdens on small businesses subject to the rule. In addition, this information would assist small entities in understanding the nature of the impact of the rule on their businesses.

Alternatives to Reduce the Impact on Small Entities

In addition to providing information about the economic impact of the action on small businesses, the RFA also requires an agency to consider less burdensome alternatives to the proposed action. In this particular rulemaking, there may be viable alternatives that HUD has not considered.

Good Faith Estimate (GFE) Provisions

Advocacy supports the notion of protecting consumers from predatory lending practices and providing the consumer with full disclosure about the mortgage lending process. Advocacy urges HUD to give full consideration to suggestions that reduce consumer confusion and are cost effective for mortgage brokers and community-based lenders.

Packaging

The purpose of packaging is to increase competition among settlement service providers and lower the cost of settlement services for the consumer. As with the GFE, Advocacy urges HUD to give full consideration to suggestions from the small business community concerning the packaging aspect of the proposal.

Conclusion

The RFA requires agencies to consider the economic impact on small entities prior to proposing a rule and to provide the information on those impacts to the public for comment. As noted above, Advocacy recommends that HUD publish a supplemental IRFA to provide small businesses with sufficient information to determine what impact, if any, the particular proposal will have on its operations. In addition to providing the public with specific information about the economic impact on the proposal, the supplemental IRFA should provide a meaningful discussion of alternatives that may minimize that impact.

Secretary Martinez, Commissioner Weicher, and members of your staff in the Office of General Counsel, deserve credit for reaching out to small businesses and consulting with my office in the development of this rule. I am confident that we will continue to work together to ensure that these improvements to the mortgage financing process stimulate small-business growth and increased opportunities for homeownership. Thank you for the opportunity to comment on this important proposal. If you have any questions, please feel free to contact the Office of Advocacy at (202) 205-6533.

Sincerely,

Thomas M. Sullivan
Chief Counsel for Advocacy

Jennifer A. Smith
Assistant Chief Counsel
for Economic Regulation

Cc: Dr. John D. Graham, Administrator, Office of Information and Regulatory Affairs

ENDNOTES

1. Pub. L. No. 96-354, 94 Stat. 1164 (1980) (codified at 5 U.S.C. § 601 et seq.) amended by Subtitle II of the Contract with America Advancement Act, Pub. L. No. 104-121, 110 Stat. 857 (1996). 5 U.S.C. § 612(a).

2. Congress established the Office of Advocacy of under Pub. L. No. 94-305 to represent the views of small business before Federal agencies and Congress.

3. 67 Fed. Reg. 49134 (July 29, 2002).

4. On October 9, 2002, the Office of Advocacy held a roundtable on this rule. Mortgage brokers, mortgage lenders, realtors, appraisers, and third party service providers participated in the roundtable. In addition, on October 25, 2002, Advocacy met with minority members of the real estate community in Baltimore, Maryland to discuss the impact of this rule on their businesses.

5. 5 U.S.C § 603.

6. 5 U.S.C. § 607.

7. Advocacy reviewed the summary of HUD's analysis published as an appendix to the proposed rule and the complete Economic Analysis and Initial Regulatory Flexibility Analysis for RESPA Proposed Rule to Simplify and Improve the Process of Obtaining Mortgages to Reduce Settlement Costs to Consumers, prepared by HUD's Office of Policy Development and Research and accessible on HUD's Website.

8. 13 C.F.R. § 121.

9. 15 U.S.C. § 632. Section 601 also provides that an agency can use an alternate definition if the agency obtains prior approval from Advocacy to use another standard (and publishes the standard for public comment) or the statute on which a rule is based provides a different definition of small business, then an agency may use that definition without consulting with the Office of Advocacy. 5 U.S.C. § 601 (3).

10. This information was obtained from http://www.sba.gov/size/sizetable2002.html.

Attachment 4

Supporting Statement for Paperwork Reduction Act Submissions

Real Estate Settlement Procedures Act Disclosures
OMB Control No. 2502-0265
(Forms HUD-1 and HUD-1A)

A. Justification

1. The Department is proposing a rule to simplify and improve the process of obtaining a home mortgage. The proposed rule will affect the current information collection, which consists of third party disclosures needed to inform homebuyers about the settlement process. Currently, certain disclosures are required by the Real Estate Settlement Procedures Act (RESPA) of 1974 amended by Section 461 of the Housing and Urban-Rural Recovery Act of 1983 (HURRA), and other various amendments. The statute is found at 12 U.S.C. 2601 et seq. and the implementing regulations at 24 CFR 3500. Required disclosures include: the Good Faith Estimate, Special Information Booklet, RESPA-Section 6 Model Disclosure and Acknowledgement of Probable Transfer of Loan Servicing, and the HUD-1 Settlement Statement. Other disclosures may be required under certain circumstances and include: the Initial Escrow Account Statement, Annual Escrow Account Statement, Affiliated Business Disclosure, and Escrow Account Disbursement Disclosure. The proposed rule would require a new format for the Good Faith Estimate. The rule would require a new disclosure, the "Guaranteed Mortgage Package Agreement," in lieu of the Good Faith Estimate, to be eligible for certain exemptions from Section 8 of RESPA. This exemption would exclude the requirement to give an Affiliated Business Disclosure in certain circumstances.

   Further explanations of RESPA, including statutory and regulatory documentation, is available through HUD's web page at **http://www.hud.gov/offices/hsg/sfh/res/respa_hm.cfm**

   Real Estate Settlement Procedures Act (Regulation X);
   Escrow Accounting Procedures
   Final Rule
   Federal Register Vol. 60 No.31 Feb. 15, 1995

   Real Estate Settlement Procedures Act (Regulation X);
   Escrow Accounting Procedures: Correcting Amendment and Clarifications
   Final Rule
   Federal Register Vol. 60 No.89 May 9, 1995

   Real Estate Settlement Procedures Act;
   Streamlining Final Rule
   Final Rule
   Federal Register Vol. 61 No.59 Mar. 26, 1996

   Amendments to Regulation X, Real Estate Settlement Procedures Act;
   Withdrawal of Employer-Employee and Computer Loan Origination Systems (CLOS) Exemptions
   Final Rule
   Federal Register Vol. 61 No.222 Nov. 15, 1996

   Amendments to Real Estate Settlement Procedures Act;
   Exemption for Employer Payments to Employees Who Make Like-Provider Referrals and Other Amendments
   Proposed Rule
   Federal Register Vol. 62 No. 90 May 9, 1997

   Amendments to Real Estate Settlement Procedures Act Regulation (Regulation X);
   Escrow Accounting Procedures
   Final Rule

Federal Register Vol. 63 No. 13 Jan. 21, 1998

Real Estate Settlement Procedures Act (RESPA);
Regarding Lender Payments to Mortgage Brokers
Statement of Policy1999-1
Federal Register Mar. 1, 1999

- HUD-1/HUD-1A - Uniform Settlement Statement. Buyers and sellers receive a statement of actual charges and disbursements pursuant to the settlement (see Section 4(a) of RESPA).

- Affiliated Business Arrangement Disclosure (formerly Controlled Business Arrangement). This disclosure is required when a settlement service provider refers a borrower to an affiliated provider. Section 461 of the Housing and Urban-Rural Recovery Act of 1983 added an exemption under Section 8 of RESPA for affiliated business arrangements (AfBAs) as long as certain requirements were met. The implementing regulations at 24 CFR 3500.15, require that a disclosure be given when a settlement service provider refers a borrower to another settlement service provider, when an AfBA exists. Proposed revisions to these regulations were published in the Federal Register on June 7, 1996 and August 12, 1996. The Department published final regulations on November 15, 1996 (effective January 14, 1997), which implement Section 2103c of the Act. The proposed rule exempts this requirement under certain circumstances.

- Special Information Booklet. Homebuyers receive this disclosure regarding the nature and costs of real estate settlement services (see Section 5(d) of RESPA).

- Good Faith Estimate (GFE). Lenders must give borrowers an estimate of the settlement costs that the borrower is likely to incur in connection with settlement (see Section 5 (c) of RESPA). The proposed rule requires a new format for the GFE that would make shopping easier. It also would require that the estimate be firmer by establishing a tolerance in variance on the HUD-1, from what was estimated on the GFE.

- Guaranteed Mortgage Package Agreement (GMPA). The proposed rule would require this disclosure in lieu of the GFE when a Guaranteed Mortgage Package, including a guaranteed settlement service cost and an interest rate guarantee is offered consumers.

- Escrow Disclosures. An initial escrow account statement is provided to borrowers at the settlement of a Federally related mortgage loan, and an annual statement is provided to borrowers showing the previous year's activities in the escrow account. The lender may ask the borrower to voluntarily contribute additional funds if the charge will substantially rise in the second year; a disclosure must be signed by the borrower. Section 924 of the Cranston Gonzalez Affordable Housing Act of 1990 (P. L. 101-625, approved November 28, 1990), amended Section 10 of the Real Estate Settlement Procedures Act of 1974 (RESPA, U.S.C. 2609 (c)). Regulations allowing voluntary collection of additional funds were published January 21, 1998, FR-3236.

- Servicing Disclosures. Lender must give the borrower a disclosure at application that the servicing of the mortgage loan may be transferred and another notice when the loan is transferred (Section 941 of the Cranston Gonzalez National Affordable Housing Act, P.L. 101-625 amended Section 6 of RESPA). RESPA was amended in 1996 to allow a streamlined disclosure, however, the Department has not finalized regulations pursuant to allow this change.

2. These third party disclosures are required by statute and regulations. Settlement providers make these disclosures to homebuyers, and in some cases sellers; pursuant to transactions involving Federally related mortgages. Disclosures are not submitted to the Federal Government.

3. These third party disclosures may be submitted to consumers electronically. Additionally, many disclosures are computer generated. The HUD-1 and HUD-1A are available on the RESPA web site and private companies offer software programs which generate HUD-1s. Except for the HUD-1 and HUD-1A, settlement providers are free to develop forms that are tailored to their individual procedures and needs. Lenders/brokers may use a computer generated program to estimate costs reported on the GFE for specific settlement services. Approximately 20,000 lenders generate an estimated 11 million loan applications which would require a GFE. It is estimated that at least 50% of the GFEs are now generated by computer. Many servicers are using integrated computer systems for billing, recordkeeping, and generating escrow statements. Software manufacturers continue to market improved versions of these systems.

4. The only disclosure containing partial duplication is the annual escrow account statement. To reduce duplication, servicers may adapt HUD-required information to comply with IRS reporting requirements regarding escrow account items, such as taxes. Furthermore, the rule allows servicers to report a "short year" in the first annual statement so that HUD-required annual statements can be issued coincident with IRS forms. In open-end lines of credit, the GFE and HUD-1 are not required when certain truth-in-lending disclosures are given.

5. The collection of this information does not impact small businesses.

6. This information is not submitted to the Federal Government. These third-party disclosures are required by statute, 12 U.S.C. 2601 et. seq. and regulations. The burdens on respondents are the minimum necessary to comply with the statute, and to assist borrowers in comparison shopping for loans and tracking escrow funds.

7. Information is not reported to HUD. Respondents are required to keep records (HUD-1, HUD-1A, escrow disclosures) for five years. Information may be requested from providers as part of an investigation. There is a three-year statute of limitations for the Secretary to bring an action under Sections 6, 8 and 9. RESPA does not provide for a statute of limitations for escrow disclosures. The Inspector General recommended a five year record retention to limit the paperwork burden.

8. The Department is soliciting comments in regard to the information collection. The Department's Office of Policy Development and Research estimates that approximately 11 million loans are originated each year. The Department is taking this opportunity to request additional burden hours to take into consideration this increase over the previous estimate in 2502-0265.

9. There are no payments or gifts to respondents.

10. There are no assurances of confidentiality provided to respondents.

11. There is no information of a sensitive nature being requested.

12. Estimated Number of Respondents, Responses and Burden Hours Per Annum

Information Collection	Number of Respondents	Frequency of Response	Responses per Annum	Burden Hour per Response	Annual Burden Hours	Hourly Cost per Response	Annual Cost
Information Booklet/GFE or GMPA	20,000	550	11,000,000	.33	3,630,000	20.00	72,600,000
HUD-1 or HUD-1A	20,000	550	11,000,000	.25	2,750,000	30.00	82,500,000
AfBA	10,000	240	2,400,000	.10	240,000	20.00	4,800,000
Initial Escrow	2,000	4,290	8,580,000	.08	686,400	*0.00	0
Annual Escrow	2,000	17,500	35,000,000	.08	2,800,000	*20.00	56,000,000
Escrow Disbursement	2,000	500	1,000,000	.083	83,000	20.00	1,660,000
Servicing Disclosure	20,000	550	11,000,000	.033	363,000	10.00	3,363,000
Transfer Disclosure	20,000	2,500	50,000,000	.033	1,650,000	10.00	16,500,000
TOTALS			129,980,000		12,202,400		$237,423K

*Cost of initial escrow is included in the annual escrow cost of $20.00, which also includes staff time, mailing cost, and equipment.

Explanation of Burden:

Good Faith Estimate, Guaranteed Mortgage Package Agreement, Special Information Booklet

- It is estimated it will take 20 minutes to complete and explain the new GFE to borrowers, or to complete and explain the GMPA to borrowers. The burden hours for these disclosure are increased due to the new formats for disclosure and to take in consideration the increased estimate of 11 million transactions rather than the previous estimate of 5 million.

HUD-1/HUD-1A

- Approximately 11 million loans close per year. The Department estimates that the HUD-1 can be filled-in in a minimum of 15 minutes. There are software programs available to settlement agents which provide an interactive form, thus allowing the form to be easily completed.

Initial Escrow Account Statement

- Approximately 11 million loans close per year, 78 percent of which carry escrow accounts requiring an initial statement (according to a HUD study), 11 million loans x .78 = 8,580,000 responses.

Escrow Disbursement Statement

- The Department estimates that 1,000,000 borrowers will voluntarily contribute additional escrow funds into accounts due to anticipated increases the second year. Servicers may collect additional funds as long as borrowers agree to do so through a disclosure. The Department estimates this disclosure will (1,000,000 x .083) result in 83,000 burden hours.

Annual Escrow Account Statement

- Thirty-one million mortgages carry escrow accounts. It is estimated that 15 percent of these mortgages change servicers each year requiring a new annual escrow account statement. Thirty-one million escrowed mortgages plus 4.65 million (15 percent of 31 million) change servicers each year equals to approximately 35 million responses. Actual responses per respondent will vary according to the number of escrowed mortgages serviced by each respondent.

Initial Servicing Disclosure

- Approximately 11 million loans are closed per year which require a disclosure, 11 million loans x .033 = 363,000 burden hours.

Servicing/Transfer Disclosures

- The transferor and transferee may send this disclosure jointly. About 50 million transfers of servicing rights are affected every year, according to a knowledgeable official at the Mortgage Bankers Association. We estimate that approximately 10% of the 50 million transfers receive a single disclosure.

Affiliated Business Arrangement Disclosure

- A settlement service provider must provide the AfBA disclosure when a borrower is referred to an affiliated provider. The Regulatory Impact Analysis estimated that 4.5% of all home sales transactions will involve an affiliated relationship (1999 sales transactions 2,400,000 x .045 = 108,000). An additional 10% of all loan applications will require a AfBA disclosure (2.4 million x .10 = 240,000).

13. There are no additional costs to respondents. Although the GMPA is a new disclosure and the format for the GFE are changed, according to private companies who provide document packages to lenders and other settlement providers, updates to state and federal regulations are provided at no additional cost.

14. There are no costs to the government except for a small cost associated with keeping the Special Information Booklet and the HUD-1 or HUD-1A up-to-date. These are third party disclosures that are not reported to the government.

15. The proposed rule provides a new Good Faith Estimate (GFE) format and provides a new Guaranteed Mortgage Package agreement that under certain circumstances may be used in lieu of the GFE. Both formats include a disclosure of options the consumer has for paying settlement costs and for lowering the interest rate. It is anticipated that these new disclosures will require additional time to complete and to explain to the consumer. Additionally, the Department is taking this opportunity to make an adjustment to increase the previous estimate of 5 million loans a year to 11 million loans a year. The adjustment is based on public comment and information provided by the Office of Policy, Development and Research. Therefore, the previous submission of 6,500,000 hours are increased to 12,202,400. Of this increase, 2,530,000 hours are attributed to a program change and 3,172,400 hours are due to an adjustment of increased loan volume.

16. The results of the information collection will not be published.

17. HUD is seeking approval to not display the expiration date on the forms HUD-1 and HUD-1A because of the very large volume that is generated. The forms are not only required by RESPA but are used for virtually all one-to-four family residential transactions and have become a standard instrument for settlement procedures throughout the industry.

18. There are no other exceptions to the certification statement identified in item 19 of the OMB 83-I than what is stated in item 17 above.

B. Collections of Information Employing Statistical Methods

The collection of information does not employ statistical methods.

AMERICAN
LAND TITLE
ASSOCIATION

TESTIMONY OF STANLEY B. FRIEDLANDER,
PRESIDENT, AMERICAN LAND TITLE ASSOCIATION
ON

"SIMPLIFYING THE HOME BUYING PROCESS:
HUD'S PROPOSAL TO REFORM RESPA"

BEFORE THE
SUBCOMMITTEE ON HOUSING AND COMMUNITY OPPORTUNITY
COMMITTEE ON FINANCIAL SERVICES
U.S. HOUSE OF REPRESENTATIVES

February 25, 2003

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My name is Stanley Friedlander and I am the President of Continental Title Agency located in Cleveland, Ohio. I am appearing today as President of the American Land Title Association[1], which represents both title insurance companies and over 1,750 title insurance agents, most of which are small businesses like mine. With me today is Ann vom Eigen, ALTA's Legislative and Regulatory Counsel.

ALTA, and I personally, would like to thank the Chair for holding these hearings. The HUD proposals may not only have a very significant and adverse impact on our industry, on our customers, and our insureds. They could also have a very negative impact on what has been the one healthy area of the American economy in recent years – the residential real estate market.

RESPA is the guiding federal regulatory program for our industry. It affects the activities of our industry, our relationships with our customers, and our relationships with lenders, real estate brokers and other settlement service providers. Indeed, no other federal statute or regulatory program has such a pervasive impact on how we do business and how we compete for business. Accordingly, ALTA and its members have been deeply involved in RESPA issues since Congress debated its enactment in the early 1970's. Over the years, we have participated extensively in every legislative and HUD regulatory forum to ensure that the RESPA rules serve the interests of consumers while providing fair and reasonable rules from the standpoint of our members.

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[1] *The American Land Title Association membership is composed of 2,300 title insurance companies, their agents, independent abstracters and attorneys who search, examine, and insure land titles to protect owners and mortgage lenders against losses from defects in titles. Many of these companies also provide additional real estate information services, such as tax search, flood certification, tax filing, and credit reporting services. These firms and individuals employ nearly 100,000 individuals and operate in every county in the country.

We understand the concerns that may have prompted the HUD proposed regulations that were published in July 2002, and believe that the Secretary and the Department deserve credit for the boldness of their initiative. However, our Association and its members are deeply concerned about how these proposals, if promulgated in final form, will impact our customers, our industry, and the real estate and mortgage lending markets throughout the country. Accordingly, we filed detailed comments on the proposed rule with HUD in its rulemaking proceeding. We also participated in an SBA roundtable on the effect of the proposal on small businesses.

What I would like to do today is highlight why we believe the proposals do not serve the interests of the consumers of our products and services, why they would adversely affect competition in our business and will particularly hurt small businesses that are the cornerstone of our industry. I will highlight an alternative we have recommended to HUD that would achieve many of the agency's objectives while minimizing consumer and industry problems. We urge the Committee to ask HUD to seriously consider these alternatives.

THE IMPACT ON CONSUMERS OF TITLE INSURANCE AND TITLE-RELATED SERVICES.

Under the current RESPA statute and regulations, lenders must provide consumers, within three business days of receiving an application, a "good faith estimate" of the closing costs the borrower "is likely to incur" in connection with the transaction. HUD is proposing to replace that regime with two alternative new regimes. The first, which is a revision of the current GFE regime, would require lenders to give less detailed estimates by category of costs, with limited or no tolerances for the accuracy of those estimates. The second regime would encourage mortgage lenders to offer what HUD refers to as a Guaranteed Mortgage Package – which would contain essentially all of the loan and other real estate-related settlement charges at a single guaranteed price, together with a loan at a guaranteed interest rate.

It appears to us that these proposals were developed with the refinance market in mind. However, it is clear that the two regimes would pose problems for consumers in purchase/sale transactions where the current homeowner is not merely refinancing an existing loan. The proposals are based on the faulty proposition that whatever services are needed by, and are good enough for the lender, will also meet the needs of the consumer. This may well be true in refinance transactions, where the settlement services obtained by the lender are intended solely to protect the lender's interest, and the borrower cares only about the total charges he or she may have to pay to obtain the loan. But it is not true in purchase/sale transactions, where the buyer and the seller have their own interests in the nature and quality of the title and closing services that are provided with regard to the conveyance of title from the seller to the buyer. HUD's proposals, particularly the GMP proposal, do not take those interests into account.

For example, the HUD proposals do not require the lender to specify what title-related services are included in the revised GFE estimate or in the GMP price, or how much of the GFE estimate or GMP price is attributable to those services. Accordingly, if the lender has decided to accept a reduced form of title protection because it believes the additional profit it will realize on the GMP as a result of the cost savings will offset the additional risk it is taking, the buyer/borrower may not appreciate that the protection the lender has decided to accept on the mortgage loan may not meet the buyer's needs with regard to the purchase transaction.

Second, because the consumer will not know what services at what costs are included in the GFE or in the GMP price, it may be impossible for the consumer to do an apples-to-apples comparison of offers from different lenders.

Third, the buyer and the seller may have agreed on the selection of the provider of certain title or closing services (such as the escrow company in states where escrow closings are customary, or a title company that will provide the title and closing services) in connection with the execution of the purchase contract and before the buyer has begun to shop for a mortgage loan. In these situations, the price of the GMP package will also include those services and the borrower could end up paying twice for the same service.

Finally, in most areas of the country the seller generally pays half of the costs for the handling of the closing and will pay for all or a significant portion of the title insurance charges for the owner's policy. In addition, it is customary in most areas for the seller to pay for the governmental charges relating to the recording of the deed (with the buyer paying the charges for the mortgage). The GMP proposal, which assumes that the buyer/borrower pays for all closing costs, completely fails to reflect these widespread seller-pay practices.

THE IMPACT ON THE TITLE INDUSTRY AND SMALL BUSINESSES IN THE INDUSTRY

The HUD proposals tilt heavily in favor of the packaging alternative, because packagers are provided an exemption from RESPA § 8 for any discounts or things of value they may receive in connection with the selection of service providers for their packages. Because a mortgage loan at a guaranteed interest rate must be part of any GMP, everyone recognizes that only lenders will effectively be able to offer packages under the HUD proposal. Accordingly, title companies and other providers of settlement services will be placed in a position where they will effectively be deprived of market access to consumers and will only be able to effectively compete by becoming part of a lender's package. This will have adverse consequences for all ALTA members, but particularly for our small business members.

Major lenders will, of course, be aware that inclusion in their GMPs may be the only effective means by which providers of title and closing services will be able to obtain any significant amount of business in residential mortgage loan transactions – or, indeed, to survive. Moreover, HUD has structured its GMP proposal in a way that mortgage lenders are in a position to realize greater profits on their GMP prices by negotiating lower prices from the providers of the services in the package. The combination of these two factors means that providers of title/closing services will face enormous economic pressure to offer cut-rate prices and/or cut-rate services in order to be selected for inclusion in lender-created GMPs.

Some of the bigger title insurers may be able to survive in this environment. But the backbone of our industry – the smaller abstractors and title agencies – will not have the resources to be able to offer the kind of discounts and payments that the larger companies can provide. Based on a survey conducted by ALTA in 2002, which was a boom year for the real estate industry, 51% of the title insurance agents and abstractors in the country had less than $500,000 in gross revenue in 2001, and 72% had less than $1 million. 68% had 10 or fewer employees, and 42% had less than 5. These individuals and companies have demonstrated that they can effectively compete with anyone for the consumer's business, but in a world in which major lenders are able to use the clout derived from the volume of transactions they handle to extract discounts from major providers, these small businesses will simply be unable to compete on that basis.

Equally important, we believe that the proposals, if implemented in their present form, would effectively close the door to future entry into this business by small businesses.

It is clear that HUD is aware of the potential negative consequences of their proposals, but believes that the adverse impact on small business is outweighed by (a) the likelihood that major lenders will be able to obtain deep discounts from major settlement service companies who will want to be part of their packages, and (b) the prospect that mortgage lenders will pass through to their borrowers the benefits of such discounts. HUD estimates that small businesses will lose somewhere between $3.5 billion and $5.9 billion in annual revenues if their proposals are implemented. Whether these estimates are accurate – or too low – is not the critical issue. The critical issues are:

- What assurances are there that lenders will pass any savings along to consumers?

- What is the basis for HUD's conclusion that the charges of our members, whatever their size, are too high and should be "squeezed" by lenders?

- Why is HUD so willing to tilt the playing field in favor of large lenders and those large settlement service providers that have the ability to provide them with significant discounts in order to be part of their packages?

- Why is HUD so cavalier about the adverse impact on small businesses, which have been a mainstay of this industry?

We have been unable to get answers on these questions from HUD, but we hope you will.

ALTA'S PROPOSAL FOR A TWO-PACKAGE APPROACH

ALTA's written comments to HUD did not merely criticize the HUD proposals. We offered a realistic alternative that we believe would achieve HUD's objectives while avoiding many of the consumer and competitive problems I have just discussed.

Our alternative is that there should be two packages:

- a "**Guaranteed Mortgage Package**" that would be offered by lenders along the lines of the current HUD proposal (or as it may be modified after the public comment period) and that would consist of: (i) a loan at a guaranteed interest rate in accordance with whatever requirements HUD ultimately determines is appropriate; and (ii) all lender-related services and charges (basically the 800 series charges on the HUD-1 form); and

- a **"Guaranteed Settlement Package"** that could be offered by any party – title insurers and title insurance agents, real estate brokers, lenders, escrow companies, or attorneys – and that would provide a guaranteed single price for all of the 1100 series services and charges (the title and related charges), the 1200 series charges (government recording and transfer charges), and those charges required for title assurance or closing purposes that may be listed in the 1300 series (miscellaneous settlement charges).

We believe this "two-package" approach would better achieve HUD's goals of (1) ensuring price certainty in the settlement process for consumers, and (2) injecting significant, "shoppable" price competition into both the lending and the settlement industries. It will help ameliorate the effects on small business because it will allow lenders and others to package on a local level. This packaging alternative will take into account the unique costs, needs, and allocation of responsibilities that exist in a local jurisdiction, and allow customization to meet consumer needs. It would also serve other important goals, such as allowing for the development of Settlement Packages in purchase/sale transactions that differ from those in refinance transactions, that would accommodate regional differences in practices, and, most importantly, would permit settlement service providers to market directly to consumers, thus preserving the competitive access of the diverse and vibrant small businesses that make up a significant part of the American settlement industry.

We also have expressed concern that the HUD proposal might freeze the way in which settlement services are delivered, and prevent the evolution of new forms of service delivery. We believe the HUD proposal would channel settlement services primarily through large lenders, thus inhibiting the development of technological and market improvements that could lead in different directions. We expressed these concerns in the Mortgage Reform Working Group in the late 1990s. Since that time, technological advances have led to dramatic improvements in consumers' access to loan and settlement services information. Many consumers now shop on line for both loan and settlement services, and some even close on line. We believe that consumers would like to continue to take advantage of these opportunities.

HUD SHOULD PROCEED SLOWLY

Finally, we, as well as other groups affected by the proposed regulations, are concerned that any reforms along the lines proposed by HUD – or even our own two-package alternative –, which would so radically affect the mortgage lending and settlement services markets throughout the United States, should not be undertaken without appropriate statutory authorization.

The revised GFE and packaging regimes constitute complex and far-ranging regulatory superstructures for which the only statutory foundation is a single sentence in § 5(c) of RESPA, enacted in the RESPA amendments adopted one year after the original statute was enacted, that requires a mortgage lender, within three business days of receiving a loan application, to provide to the applicant a "good faith estimate of the amount or range of charges for specific settlement services the borrower is likely to incur." That slim statutory foundation will not support such weighty regulatory measures as HUD is proposing, no matter how well intentioned they may be. Moreover, the original RESPA statute contained provisions for the kind of firm estimates of closing costs that HUD has proposed, but these provisions were repealed in the 1975 amendments in which the "good faith estimate" language was adopted.

We believe that, irrespective of whether one believes that the HUD proposals are good or bad, or workable or unworkable, this Committee and the Congress should be concerned about HUD's implementing such changes without clear legislative authority.

First, there is a significant question of public policy at issue here – whether modifications of such proportion that will so fundamentally affect a major segment of the American economy should be implemented without legislative direction and authorization.

Second, the HUD regulations could well be challenged in the courts and the legal uncertainty regarding whether they will be upheld or struck down will, by itself, cause significant disruption in the real estate and mortgage lending markets. The HUD proposals, if adopted, will require massive and costly efforts by all parties in the residential real estate and mortgage lending industries to restructure their business arrangements, modify their forms and software, retrain personnel, etc. Much of that effort and costs to accommodate to the new regulations would be rendered useless if, after the regulations are promulgated in final form, the courts find – as our lawyers tell us is likely – that the regulations are unauthorized and cannot be enforced. Many Federal agencies, faced with this type of situation issue reproposed rules. This process would allow the agency to address concerns expressed in comments on the original rule, modify their original proposal, and allow industries and affected parties to further analyze a revised proposal. This would provide substantial benefits.

In short, this is not an issue where we – or the Congress – can afford to say "let's see how the courts come out on this." Our members and the real estate and mortgage markets need greater certainty that any final regulations adopted by HUD will not be found to be unauthorized. We urge this Committee and the Congress not to allow such uncertainty to be created.

October 28, 2002

Rules Docket Clerk
Office of General Counsel
Room 10276
Department of Housing and Urban Development
451 Seventh Street, S.W.
Washington, D.C. 20410-0500

RE: Proposed Rule on Real Estate Settlement Procedures Act (RESPA); Simplifying and Improving the Process of Obtaining Mortgages To Reduce Settlement Costs to Consumers; Docket No. FR-4727-P-01; 67 Fed. Reg. 49134 (July 29, 2002)

Dear Sir or Madam:

We are writing to supplement our October 4, 2002 comments with additional information on the effect of the proposed rule on small businesses within our industry. On October 9, 2002, Carla Detring, ALTA's Immediate Past President, and President of Preferred Land Title of Farmington, Missouri, participated in a roundtable at the Small Business Administration on the possible effects of the proposed rule on small businesses. This submission summarizes the points made during that discussion.

The American Land Title Association, represents over 1600 title insurance agents, most of which are small businesses. The title and settlement services industry has traditionally been an industry in which there have been few barriers to entry by small businesses and in which small businesses have thrived. This is due in part to the local nature of our business – serving the needs of customers in local real estate transactions – and to the fact that we are also a highly service-oriented business where meeting the needs of local customers has been an important factor, in addition to having competitive fees.

In fact, our most recent statistics[1] indicate that around 36% of our agent members have total annual gross revenue of less than $250,000, while 60% have total annual gross revenue of less than $500,000. One-half of the companies responding to our most recent survey have between three and 10 full time employees. One-fourth have three or fewer full time employees.

We believe that the HUD proposed revisions to the RESPA regulations, particularly the Guaranteed Mortgage Packaging proposal, would have a very serious adverse effect on these small businesses in the our industry, and on their ability to compete for consumer business. Equally important, we believe that the proposals, if implemented in their present form, would effectively close the door to future entry into this industry by small businesses.

[1] Fetzer-Kraus, Inc. ALTA Abstracter and Title Agent Operations Survey, 2001

It is clear that HUD is aware of these consequences, but believes that the adverse impact on small business is outweighed by (a) the likelihood that major lenders will be able to obtain deep discounts from major settlement service companies who will want to be part of their packages, and (b) the prospect that mortgage lenders will pass through to their borrowers the benefits of such discounts. HUD estimates that small businesses will lose somewhere between \$3.5 billion and \$5.9 billion in annual revenues if their proposals are implemented. Whether these estimates are accurate – or too low – is not the critical issue. The critical issues that HUD should be focusing on follow.

- Does the proposed rule tilt the playing field in favor of large lenders and those large settlement service providers that have the ability to provide them with significant discounts in order to be part of their packages?

- Does the proposed rule disproportionately impact small title and settlement service businesses, which have been a mainstay of this industry, an industry that has provided opportunities for employees of larger companies to strike out on their own and develop their own businesses?

We believe that the HUD proposal will undermine the role of small business in the title and settlement services industry for several reasons.

First, because of the incentives HUD has provided for packaging, it is clear that the market will move substantially in that direction, rather than towards the revised good faith estimate (GFE) regime.

Second, while HUD maintains that "anyone can provide packages," under its proposed Guaranteed Mortgage Package regime, the GMP Agreement offered to consumers must include a loan at a guaranteed interest rate. It is thus highly unlikely that anyone other than lenders will be in a position to effectively offer GMPAs. The mortgage lending industry has become increasingly concentrated – in the last 5 years the top 10 mortgage originators have doubled their market share from 25% to 50% – and the HUD packaging proposal will have the effect of increasing the concentration in the title and settlement services industry.

Third, by granting a broad exemption from RESPA § 8 for its GMPA proposal, HUD is encouraging lenders to seek, and settlement service providers to offer, discounts and other benefits in order for the providers to be included in the lenders' packages. In that kind of environment – where the lender rather than the consumer is going to make the choice of provider – the bigger title and settlement service companies are far better positioned to offer such discounts and inducements than the small business provider.

Fourth, if the packaging regime becomes widespread, as is likely to happen because it has the backing of the major mortgage lenders in the country, providers of title and settlement services will only be able to market their services to and through lenders. The competitive advantage of small businesses – service to the consumer – will be undermined. Likewise, there will be fewer competitive opportunities for new small businesses to enter this market since the only way they will be able break into the market will be to offer even greater discounts to lenders than they can obtain from the major settlement service companies. This is unlikely to happen.

In sum, while there may be certain consumer benefits in the packaging concept, the current HUD packaging proposal must be modified as suggested in our October 4 submission so as to ensure that any provider, including small businesses, will be able to have effective access to the market other than through mortgage lenders.

Please feel free to contact us if we can be of any other assistance.

Sincerely,

James R. Maher

AMERICAN
LAND TITLE
ASSOCIATION

October 4, 2002

Rules Docket Clerk
Office of General Counsel
Room 10276
Department of Housing and Urban Development
451 Seventh Street, S.W.
Washington, D.C. 20410-0500

RE: Proposed Rule on Real Estate Settlement Procedures Act (RESPA); Simplifying and Improving the Process of Obtaining Mortgages To Reduce Settlement Costs to Consumers; Docket No. FR-4727-P-01; 67 Fed. Reg. 49134 (July 29, 2002)

Dear Sir or Madam:

These comments on the above-referenced proposed rule are respectfully submitted on behalf of the American Land Title Association ("ALTA" or "the Association"), the national trade association of the land title industry.[1]

Our association and its members commend the Department for the objectives it is seeking in the bold proposals contained in the proposed rule and support those objectives – to ensure that consumers are provided understandable and reliable information on the costs of mortgage loans and settlement services as early in the real estate/mortgage

[1] The American Land Title Association membership is composed of 2,400 title insurance companies, their agents, independent abstracters and attorneys who search, examine, and insure land titles to protect owners and mortgage lenders against losses from defects in titles. Many of these companies also provide additional real estate information services, such as tax search, flood certification, tax filing, and credit reporting services. These firms and individuals employ nearly 100,000 persons and operate in every county in the country.

lending transaction as possible so that they can effectively shop for such loans and services, to simplify the disclosures currently required by RESPA, and to eliminate surprises at closing. Those objectives are consistent with the policy statement on RESPA reform adopted by the Board of Governors of the Association:

> ALTA supports settlement services legislation or regulations that promote consumer choice and empowerment and require meaningful disclosure. ALTA recognizes that the consumer has a separate benefit or interest in the selection of the product or service of each component in the package.

We are, however, deeply concerned about certain aspects of the proposals, and believe that the proposals as currently structured would adversely affect buyers and sellers of real estate, as well as ALTA's members. However, because we are in agreement with many of HUD's objectives, this submission not only discusses the problems we perceive with HUD's proposed approaches, but offers a suggested alternative that we believe meets those objectives without the attendant problems in the current HUD proposals.

More fundamentally, we believe that any reforms along the lines proposed by HUD, which would so radically affect the provision of, and competition for, mortgage lending and settlement services throughout the United States, cannot and should not be undertaken without appropriate statutory authorization. The revised good faith estimate (GFE) and Guaranteed Mortgage Package Agreement (GMPA) regimes proposed by the Department (as well as the proposed approach we are suggesting in Part III of this submission) constitute complex and far-ranging regulatory superstructures for which the only statutory foundation is a single sentence in § 5(c) of RESPA, enacted almost three decades ago, that requires a mortgage lender, within three business days of receiving a loan application, to provide to the applicant a "good faith estimate of the amount or range of charges for specific settlement services the borrower is likely to incur." That slim statutory foundation will not support such weighty regulatory measures, no matter how well intentioned they may be. In our view, implementation of such measures requires further legislation.

These comments are organized as follows. Part I discusses some of the major concerns that we have with the GFE and GMPA proposals and the misperceptions about title and closing-related services that we feel underlie those proposals. This discussion provides relevant context for the explanation presented in Part II of why we believe the proposals – particularly the GMPA proposal – would have unfairly adverse consequences on our industry and on consumers we serve in residential real estate transactions. Part III then presents an alternative approach to the GMPA proposal that ALTA believes would achieve all of the fundamental objectives sought by HUD without the attendant adverse consequences identified in Part II for the title-related industry and for consumers. Finally, Part IV provides comments on particular aspects of the proposals and responds to a number of the questions on which the Department asked for comment.

To facilitate the Department's review of this submission, a table of contents appears on the following pages. The table of contents will serve as an executive summary of the major points made in this submission.

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I. ALTA'S SIGNIFICANT CONCERNS ABOUT THE HUD PROPOSALS AND MISPERCEPTIONS THAT MAY BE UNDERLYING THE PROPOSALS.

Before addressing our concerns regarding particular aspects of the proposals, it will be helpful to the Department to discuss the broader concerns we have about the proposals and some misperceptions that we believe have influenced the Department's thinking on the proposals.

A. Not Only Are HUD's Far-Reaching Proposals Not Authorized By The Current RESPA Statute, The Legislative History Of The RESPA Provision On Which HUD Bases Its Proposals Demonstrates That Congress Expressly Rejected The Kind Of Firm Estimates Of Settlement Costs That HUD Wants To Require.

The changes being proposed by the Department to the RESPA regime are the most extensive and significant since the statute was first enacted in 1974. Unlike the affiliated business arrangement regulations, which implemented the 1984 controlled business amendments, the Department is proposing to change the way in which settlement services are marketed, priced, and delivered without any statutory authorization or direction. As discussed below, not only does this raise a significant legal issue regarding HUD's authority (which, if not remedied, will ultimately undermine enforcement of the new regulatory regimes), it also raises questions of sound governmental policy – whether modifications of such proportion that will so fundamentally affect a major segment of the American economy should be implemented without legislative direction and authorization.

1. The sole statutory authority for the HUD proposals is a single sentence in the Act, which does not authorize the kind of regulatory regimes being proposed and was enacted as part of the 1975 amendments that repealed provisions in the original RESPA that contemplated the kind of regimes HUD now seeks to recreate.

The sole statutory authorization for both the GFE and GMPA proposed regimes is a single sentence in section 5(c) of RESPA, 12 U.S.C. § 2604(c), that requires a mortgage lender, within three business days of receiving a loan application, to provide to the applicant a "good faith estimate of the amount or range of charges for specific settlement services the borrower is likely to incur."[2] While this sentence specifies that lenders must provide these estimates in good faith, it does not require that they undertake any specific commitments with regard to these estimates, nor does it require that lenders or other settlement service providers limit their charges to conform to any estimates provided. Indeed, the enactment of the § 5(c) good faith estimate requirement was part of the 1975 amendments to RESPA that expressly repealed the requirement in the original statute for advance disclosure to consumers of the actual settlement costs they would be incurring.

[2] While HUD is also attempting to use its authority under RESPA §§ 8(c)(5) and 19 to create "safe harbors" from § 8 liability for parties who comply with its proposed GMPA regime, those sections do not provide statutory authorization for the GMPA or GFE regimes. In particular, the use of this exemption authority to create a "carrot" (to induce packaging) and a "stick" (to ensure that parties comply with HUD's GMPA regulations by providing that failure to comply will result in exposure to § 8 violations) is not consistent with Congress' objectives in providing HUD with the §§ 8(c)(5) and 19 authority.

a. The GFE and GMPA regimes primarily govern the charges that can be imposed at settlement, rather than the "estimates" of settlement costs that may be incurred.

The behavior being addressed by the HUD proposals has less to do with a lender's good faith "estimates" of what settlement costs are likely to be than it has with the amounts that can be charged at settlement. The fact that the behavior being regulated by the proposals is the pricing of settlement services, not the provision of estimates, is reflected in the "penalties" HUD is proposing to create for violations of its new regimes.

As will be discussed below, Congress expressly decided not to impose any sanctions for violations of the good faith estimate requirement in §5(c). To overcome this statutory "shortcoming," HUD is proposing that violations of its new GFE regime result in a consumer's being able to "walk away" from the loan application and settlement, and to recover any amounts previously paid to the lender.[3] With regard to the GMPA regime, HUD's "sanctions" to ensure compliance is to make the GMPA an agreement enforceable under state law and to provide that the § 8 safe harbor will be lost if the conditions for the GMPA are not met (*i.e.*, lenders, packagers, and providers of services in the package would become subject to § 8 sanctions and lawsuits for the discounts, mark-ups and other pricing practices that are contained in the GMPA).[4] In both situations, <u>it is the pricing of settlement services at the closing rather than the estimates initially provided that triggers the violations</u>.

[3] Proposed § 3500.7(d)(1). The proposed regulations do not cite any statutory basis for HUD's creation of such a right.

[4] Proposed §3500.16(b).

In the original RESPA statute as enacted in 1974, Congress provided for a regime of advance disclosures by lenders of the actual charges to be incurred by the borrower at settlement, enforceable through liability for civil damages for failure to provide the requisite disclosures. As discussed next, that provision was repealed in 1975 and the current language of § 5(c) was substituted in order to undo the "unworkable" and "overly rigid" requirements of the original provision, which Congress concluded were "neither necessary nor, as experience has borne out, desirable."[5]

b. The legislative history of the good faith estimate requirement in § 5(c) – which was accompanied by Congress's repeal of the original § 6 of RESPA that provided for advance disclosures of the actual charges to be incurred – demonstrates that § 5(c) does not authorize the proposed HUD regimes.

As part of the original RESPA statute, Congress enacted a separate section entitled "Advance Disclosure of Settlement Costs" which required lenders, at the time of the loan commitment but not later than 12 days prior to settlement, to provide to the prospective buyer and seller an "itemized disclosure in writing of each charge arising in connection with the settlement."[6] The section imposed a duty on the lender to obtain from persons who were to provide services in connection with the settlement "the amount of each charge they intend to make." If the exact charge was not available, a good faith estimate could be provided. Section 6(b) provided for lender liability to the buyer and/or seller for failing to provide the requisite disclosures in the amount of actual damages or

[5] H.R. Rep. No. 94-667 at 2, 4 (1995), *reproduced in* 1975 U.S.C.C.A.N. 2449, 2451.

[6] Sec. 6 of the Real Estate Settlement Procedures Act, Pub. Law 93-533 (Dec. 22, 1974).

$500, whichever was greater, plus, if the action was successful, court costs and attorney's fees.

Concerns about this provision (and several others in the original RESPA legislation) were raised by lenders, with the result that, within one year of enactment, Congress repealed section 6 and substituted for it the language of § 5(c) requiring lenders to provide a good faith estimate of settlement costs (along with the HUD Special Information Booklet) within three days of a loan application.[7] Pointedly, and unlike the repealed § 6, Congress decided not to impose any sanctions for violations of this § 5(c) obligation.

Rep. Leonor Sullivan (D. Mo.) filed dissenting views to the committee report in which she argued that the repeal of § 6 would repeal the "most important provision – the heart of the law."[8] She went on to decry that "in repealing Section 6, the bill eliminates any penalty whatsoever for failure to give information which is, in fact, a 'good faith' estimate. And it will be only when the buyer goes to settlement that he or she will learn *exactly* what settlement charges are being required."[9]

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[7] Pub. Law 94-205 (Jan. 2. 1976). The report of the House Committee on Banking, Housing and Urban Affairs described the problems created by §6's requirement for lenders to determine and disclose the "exact amount" of each settlement charge under "rigid time constraints" and indicated that the amendment made by the committee to § 5(c) imposed a more general requirement "for the lender to include with the special information booklet a good faith estimate of the amount or range of charges for specific settlement services the prospective borrower is likely to incur in connection with the settlement." H.R. Rep. No. 94-667 at 4-5 (1975), *reproduced in* 1975 U.S.C.C.A.N. 2451-52.

[8] *Id.* at 18, 1975 U.S.C.C.A.N. at 2459.

[9] *Id.* at 18-19, 1975 U.S.C.C.A.N. at 2459 (emphasis in original).

In short, the kind of disclosure regimes HUD is now proposing – requiring firm disclosures of what the actual charges for settlement services will be, backed by sanctions for lenders who fail to abide by such disclosures – was, at one time, authorized by Congress in RESPA, but that authorization was repealed in 1975. In the face of that legislative history, it cannot be contended that the proposed regimes are authorized by the good faith estimate language of § 5(c) or consonant with Congress's legislation on the subject.

2. There are other reasons why legislation is needed to authorize the proposed regimes.

Because Congress has not provided appropriate penalties or liabilities for violations of § 5, HUD has had to create proposed sanctions for violations of the GFE and GMPA requirements. These sanctions are inappropriate or counterproductive, and further demonstrate the need for an appropriate statutory foundation – with appropriate sanctions – to support the regulatory approaches HUD believes are desirable.

The proposed sanction for violation of the new GFE requirements – a right for the consumer to walk away from the transaction at closing and to recover any amounts previously paid – is an administrative creation that is unlikely to be effective. It is doubtful that many consumers, facing charges at settlement that may be somewhat higher than the GFE category estimates, would walk away from the transaction, even if they were entitled to recover fees they had paid to date.

The proposed sanction for violations of the GMPA regime – loss of the § 8 safe harbor – places lenders and settlement service providers who participate in packages in an impossible position. To create the GMPAs offered to consumers, lenders and settlement service providers (such as ALTA's members) are encouraged to engage in behavior – the offering of discounts or inducements to the lender/packager, the packager's mark-up of other provider's services, and/or the required use of an affiliated business entity's services – that HUD believes violate §§ 8(a) and (b) and for which it is providing a safe harbor. But any failure of a packager to comply with all of the detailed requirements of the proposed GMPA regime will result in a loss of the safe harbor and the exposure of all the parties who have been involved in the package to § 8 liability. This is certainly not the kind of sanction or liability that Congress would create as part of a rational legislative scheme for packaging, but it is the kind of sanction HUD is forced to resort to when it has no statutory backing for its regulations.

Moreover, we believe that the HUD proposals have a significant impact on the operation of other statutes, such as the Truth in Lending Act (TILA) and the Home Owners Equity Protection Act (HOEPA), and changes would be needed to those other statutes to accommodate aspects of the HUD GFE and GMPA proposals.[10] For example, both of those statutes are dependent on itemization of specific settlement costs, some of which are included in the "finance charge" under TILA (or the "points and fees" under HOEPA), and others of which are excluded. HUD's GMPA proposal (and, to a lesser extent, the GFE proposal) would provide for a single price without any disclosure to the consumer of the charges attributable to individual settlement services in the package.

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[10] In addition, there will be a need to resolve the inconsistencies between the proposals and current FHA program limitations on the amount of fees that can be paid by the purchaser.

This will make it difficult or impossible in many cases to verify the finance charge or APR in the TILA context, or to determine whether the HOEPA thresholds for coverage under that act have been triggered by the terms of the loan.

Equally significant, TILA and HOEPA clarification is needed to make clear how the lender's profit on the GMP is to be taken into account in determining the finance charge and the HOEPA "points and fees."

Finally, we would note that, for more than 25 years, HUD and the market have operated under the current HUD regulations for the provision of good faith estimates, which HUD cannot deny are consistent with the statutory commands of RESPA § 5(c). HUD's proposed regulations do not indicate whether – and, if so, why – a lender who decides to continue operating under the current regulations after the date the new proposals become effective would be in violation of RESPA § 5(c). While Congress has the constitutional power to amend RESPA to declare that such disclosures are no longer permissible after a specified date, it is an open question whether HUD has the regulatory power, absent changes to the statute, to render unlawful disclosures and estimates that have been lawful for a quarter of a century.

3. **Apart from the legal reasons why statutory authorization is needed, HUD should not embark on such a major restructuring of the mortgage and settlement services markets without Congress's support and direction.**

The residential real estate sector constitutes a critical – and currently healthy – component of the American economy. As HUD itself has recognized, "the American mortgage finance system is justifiably the envy of the world."[11] HUD's proposals would effect dramatic changes in that sector with anticipated and unanticipated consequences that could easily impair the healthy functioning of that sector. Such changes, and the risks they entail, should not be undertaken in the absence of full public debate and clear Congressional authorization and direction.

Moreover, it would be a potential administrative nightmare if HUD were to proceed to the promulgation of final regulations on the GFE and GMPA proposals, the market began to implement the proposed regimes, and the courts thereafter concluded that HUD lacked the statutory authority to promulgate the regulations. While HUD could avert this problem by having any such challenges resolved prior to the effective date of the regulatory changes, this could take several years. The resolution to this dilemma is clear. HUD should not proceed in the absence of appropriate statutory authorization.

ALTA's position that such significant changes as are being proposed by HUD should only be effected through legislation should come as no surprise to the Department. Essentially all of the major aspects of the current GFE and GMPA proposals are taken from the July 1998 Joint Report to the Congress Concerning Reform to the Truth in Lending Act and the Real Estate Settlement Procedures Act prepared by the Board of Governors of the Federal Reserve System and the Department.[12] The very first page of the Executive Summary of that Joint Report indicated that "[i]n 1997, the agencies

[11] Introduction to HUD's RESPA proposals, 67 Fed. Reg. at 49134.

[12] The report is available at http://www.federalreserve.gov/boarddocs/rptcongress/tila.pdf.

concluded that meaningful change could only come through legislation. This report presents the Board's and HUD's recommendations for revising TILA and RESPA."

In short, HUD itself has recognized that the kind of changes it would like to see made in the disclosure and packaging of settlement costs necessitates statutory amendments to RESPA.

B. The Proposals, Particularly The GMPA Proposal, As They Would Apply To Title And Closing-Related Services, Are Based On Certain Misperceptions About These Services.

ALTA believes that several fundamental misperceptions about title and closing-related services underlie HUD's proposed treatment of those services in both the GFE and, in particular, the GMPA proposals. ALTA's concerns regarding the impact of the proposals on buyers and sellers of real estate and on the title industry, which are discussed in Part II of these comments, will be better understood by highlighting what we believe are the significant misperceptions that give rise to those concerns.

1. Misperception # 1: "What's good enough for the lender is good enough for the consumer."

HUD's proposals appear to reflect the view that all settlement charges, including title and closing-related services, are needed and purchased only because of lender requirements or are really provided for the lender's benefit. Accordingly, in HUD's view consumers have essentially no interest in who provides such services and it is therefore appropriate to have the lender bear responsibility for the selection of the providers of these services and for the amounts to be charged for these services. The consumer's only interest is the lowest total price for closing the loan and settling the real estate transaction.

While HUD is correct with regard to lender-imposed charges (such as application fees, origination fees, and charges for lender review of documents) or third-party services provided to the lender that the consumer would not otherwise have to purchase or pay for in the absence of a mortgage loan (*e.g.*, credit report, appraisal, tax report, and flood certification), HUD's view is wrong with regard to title-related and closing services, at least in transactions involving the purchase and sale of property. In those transactions, which frequently involve the most significant investment and transaction a consumer ever engages in, title and closing services are provided for the primary benefit of the buyer and the seller, are intended to protect or advance their interests, and would be purchased in such transactions even if there were no mortgage loan.[13] Accordingly, buyers and sellers have a real interest in the nature and quality of the title and closing services provided in connection with that transaction. For that reason, buyers and sellers have the right to select who will provide those services.

The Department appears to believe that a buyer's sole interest in the 1100 series services is an elective decision whether to purchase owner's title insurance, and, apart from that decision, all of the other interests of the buyer and the seller in the handling of the transaction will be adequately served if the lender's needs are met and if the providers of all the services are selected by the lender. That is not the case. Indeed, just the opposite is true. So long as the lender's advance of funds to a title insurance agent is

[13] In this regard, it deserves noting that section 106(a) of the Truth in Lending Act, 15 U.S.C. § 1605(a), defines "finance charge," which is used to calculate the annual percentage rate (or APR) on a loan, to <u>exclude</u> "charges of a type payable in a comparable cash transaction." This is in recognition of the fact that these are services needed by the buyer and seller irrespective of whether a mortgage loan is involved in the transaction.

covered by a Closing Protection Letter (or "Insured Closing Letter" as it is sometimes called) from a title insurer[14] and, when the transaction is closed, by a loan title insurance policy, the lender's interests are adequately protected.

Providers of title and closing services must meet the needs of all of the parties to the transaction, including the buyer, the seller, and the lender. Having such providers beholden to the lender for their selection and payment will inevitably result in the interests of the lender being placed ahead of the interests of the buyer and the seller. This is not something that HUD should be encouraging.

2. Misperception # 2: Consumers do not need to know what title and closing-related services are being provided in the GFE or GMPA proposal of a particular lender, or what portion of the total Category III(D) or GMPA price is attributable to these services.

The HUD proposals reflect the view that consumers do not need to know what services are being provi ded or at what prices, and that all of the consumer's interests are served by just knowing the total amount she will have to pay for 1100 series charges (in the GFE proposal), or the total amount of all settlement costs (in the GMPA proposal). As will be discussed in Part II, below, this is not the case and the failure of the proposals to provide such information will adversely impact buyers and sellers.

[14] A Closing Protection Letter is given to a lender by a title insurance company in which the company agrees to be responsible if the closing agent does not follow the lender's instructions or misappropriates the loan proceeds. Lenders usually require such a letter to be on file for each settlement.

3. Misperception # 3: Buyers pay for all settlement services.

HUD assumes that it is the buyer who pays for settlement services so that having the lender package and guarantee the price for such services to the borrower will reduce the costs the borrower would otherwise have to pay. The fact is, however, that in almost all areas of the country outside the mid-Atlantic states sellers pay for a substantial portion of the title-related charges (such as the owner's title insurance policy) and share the charges for the handling of the closing (including, in the western United States where escrow closings are customary, the handling of the escrow). Moreover, because of limitations in FHA-insured transactions on the settlement costs that can be paid by buyers, sellers in such transactions invariably pay for certain costs that are not permitted to be paid by the buyer. HUD's proposals do not take these seller-pay practices into account.

4. Misperception # 4: Owner's title insurance is always a mere add on to the issuance of the loan title insurance policy.

HUD's proposals appear to assume that the title insurance policy issued to protect the lender (referred to in the industry as the "loan policy") is the primary determinant of the title insurance price and that the issuance of the owner's policy is an "add-on" to the transaction. While this may be true in residential real sale transactions in the eastern United States, it is not the case in transactions in most other parts of the country, where the issuance of the loan title insurance policy is the "add-on" to the primary title insurance charge for the owner's policy.

C. The HUD Proposals Are Structured So As To Make It Highly Likely That The Market Will Move Towards Lender-Provided Packages.

While HUD may believe that (a) both the GFE and GMPA regimes will be adopted and readily available in the market, and (b) any party will be able to offer GMPAs, because of the way in which the proposals are structured it is highly likely that the market will gravitate toward the GMPA regime, and only mortgage lenders will effectively be able to market GMPs to consumers, with title companies and other settlement service providers becoming elements of the package or, at most, subpackagers to mortgage lenders.

1. The incentives provided for packaging will ensure that lenders favor the GMPA regime over the GFE regime.

For two reasons, we believe that the GMPA approach is likely to be far more attractive to mortgage lenders than the GFE regime and, hence, that the market will move strongly in that direction.

First, the "safe harbor" from RESPA § 8 proposed for the pricing of the GMP and for services offered within the GMP provides a huge incentive to lenders to adopt that regime. Under the GFE regime as proposed, lenders must pass through to the consumer all discounts in prices that are offered by settlement service providers in order to be recommended by the lender. Because of the continued application of § 8 lenders will not be able to accept things of value or other benefits from such providers who want to be on their "recommended" list, nor will they be able to require the use of their affiliated provider. In contrast, the § 8 exemption that is offered by HUD to lenders who adopt the GMPA regime would enable lenders to profit from the difference between the price they can charge for the GMP and the costs they must incur for the services in the package, they can obtain payments or other things of value from providers who want to provide services for their packages, and they can require the use of an affiliated provider without having to comply with any of the three safe harbor requirements for affiliated business arrangements.

Second, the effort and cost to a lender of developing and pricing the GMP is not substantially different from the effort and cost that would be involved in developing the information needed to provide the guaranteed "estimates" in the GFE.

The combination of these two factors will make it highly likely that lenders will favor the GMPA approach rather than the GFE approach.[15]

2. The GMPA regime proposed by HUD makes it unlikely that anyone other than lenders will be in a position to offer GMPAs.

While HUD's proposal appears to allow anyone to offer a GMPA, because the GMPA must include a loan at a guaranteed interest rate it is unlikely that anyone other than lenders will be in a position effectively to offer a GMPA to consumers. While lenders may turn to third parties, such as title companies, to help put together some or many of the services the lender requires for the package, because the GMP must also include all of the charges the lender may be seeking in connection with the origination of the loan, a non-lender packager cannot establish the single charge for the package without

[15] We understand that there may be certain aspects of the GMPA regime that lenders may find objectionable (such as the linkage of any change in the interest rate offered to a verifiable and independent index), but assume that, in light of HUD's clear preference for the GMPA regime, it will find a way to correct any such problems.

knowing the origination and other lender-retained charges that particular lenders will want to realize in the transaction. Moreover, even where a lender may be willing to team up with a title company or other non-lender party to offer GMPAs on a joint basis, the final price of the GMP offered to applicants is likely to be determined by the lender.

HUD's explanation of the GMPA proposal states that if an entity other than a lender decides to offer a GMPA, then both the non-lender entity and the lender must sign the GMP. While HUD's explanation suggests that the non-lender packager could have a lender sign the GMPA after the borrower has accepted the GMPA, as a practical matter it is difficult to see how a non-lender entity would run the risk of offering a GMPA to a borrower – and thereby become obligated to provide both the loan and the GMP at the guaranteed prices – without having gotten the commitment from a lender to provide the loan portion of the GMPA. Moreover, the information that has to be completed on page 2 of the GMPA form[16] with regard to the terms of the loan and the alternative options regarding the payment of up-front settlement costs and interest rates may be impossible for a non-lender to complete.

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With this background, we will now explain why we believe that the GMPA proposal (and, to a lesser extent, the GFE proposal as well) – as it applies to title and closing-related services – poses significant concerns for consumers and for the title industry.

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[16] *See* 67 Fed. Reg. at 49169.

II. THE REGIMES AS PROPOSED WOULD CREATE PROBLEMS FOR CONSUMERS IN PURCHASE TRANSACTIONS AND WOULD UNREASONABLY AND ADVERSELY IMPACT THE TITLE INDUSTRY.

A. The Problems Posed for Consumers.

Because title and closing-related services are provided for the benefit of the buyer and seller, such services and charges cannot be treated in the GFE and GMPA proposals in the same way as those services that are provided for the exclusive benefit of the lender.

As discussed in Part I.B., above, HUD's proposals with regard to the 1100 series charges fail to take into account that buyers and sellers of residential real estate have an interest in the selection of providers of title-related and closing services that is not necessarily co-incident with the interest of the lender.[17] Accordingly, we can understand HUD's view that buyers and sellers have little or no interest in what kinds of services are provided exclusively to the lender or who provides those services, and that consumers care only about the total charges they have to pay for such lender-related services. For the following reasons, however, that is not the case with regard to title and closing-related services.

[17] For example, because of their sophistication, financial resources, and ability to handle financial risk, mortgage lenders may be able to operate without traditional forms of title-related protection or services, and self-insure some or all of the title-related risks in connection with the loans they make if that will reduce their costs in providing GMPAs and increase their profitability. On the other hand, a consumer who purchases a parcel of residential real estate cannot on her own spread her risk in that transaction among thousands of other transactions nand needs to have the protection of title insurance and appropriate title-related services if she wants to (a) be certain of the nature of the title being obtained from the seller (and any limitations or liens that may exist against that title), and (b) ensure that her use and enjoyment of the property will not be disturbed by the assertion of undisclosed liens, claims or encumbrances against the property,.

First, the HUD proposals do not require the lender to specify what title-related services are included in the Category III(D) estimate or in the GMP price, or how much of the estimate or GMP price is attributable to those services. Accordingly, if the lender has decided to accept a reduced form of title protection because it believes the additional profit it will realize on the GMP as a result of the cost savings will offset the additional risk it is taking, the buyer/borrower may not appreciate that the protection the lender has decided to accept on the mortgage loan may not meet the buyer's needs with regard to the purchase transaction.

Second, because the consumer will not know what services at what costs are included in the GFEs or in the GMP price, it may be impossible for the consumer to do an apples-to-apples comparison of offers from different lenders. For example, in the GFE context, two lenders may provide the same estimate for Category III(D) services, but Lender A may be using a non-traditional form of loan title protection that will require the borrower on her own to pay for the kind of title search, title examination, and title assurance needed to protect her interests in the purchase of the home, whereas Lender B's Category III(D) charge may include the kind of title search and examination on the basis of which an owner's title insurance policy may be issued (in which case the buyer would only have to pay on her own for the owner's title insurance policy). In the GMPA context, this problem is even worse because all closing costs and settlement charges are lumped into a single figure.[18] Accordingly, in shopping among various lenders, there is

[18] Accordingly, a lender who has overestimated the government recording fees and transfer taxes that will ultimately be paid in the transaction may appear to be a "higher cost

no way for the buyer/borrower to determine what costs have been attributed to what elements of the package.

Third, the buyer and the seller may have agreed on the selection of the provider of certain 1100 series services (such as the escrow company in states where escrow closings are customary, or a title company that will provide the title and closing services) in connection with the execution of the purchase contract and before the buyer has begun to shop for a mortgage loan. In these situations, the price of the GMP package will also include those services and the borrower could end up paying twice for the same service.[19]

Fourth, in most areas of the country the seller generally pays half of the costs for the handling of the closing and will pay for all or a significant portion of the title insurance charges for the owner's policy. In addition, it is customary in most areas for the seller to pay for the governmental charges relating to the recording of the deed (with the buyer paying the charges for the mortgage). The GMP A proposal, which assumes that the buyer/borrower pays for all closing costs, completely fails to reflect these widespread seller-pay practices. If GMPAs do not provide an itemization of the 1100 and 1200 series services contained in the GMP price being offered, the buyer/borrower could end up having to pay for services that sellers currently assume.

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lender," even if the components of its package involving third-party services are lower than those of other lenders.

[19] In the GFE context, failure to disclose the individual elements of the Category III(D) estimate so that the buyer/borrower can determine what the total estimate would be <u>without the inclusion of those services she has separately arranged to purchase</u> could lead the consumer to select the lender offering the highest prices for the remaining services, not the lowest.

B. The HUD Proposals Would Effectively Deprive ALTA Members Of Direct Access To The Consumer Market With Likely Adverse Consequences for The Industry.

The GMPA regime, which, as discussed above, lenders are almost certain to adopt because of the incentives created by HUD, would effectively limit the ability of providers of title and closing services to compete directly for the consumer's business, even in purchase/sale transactions. Rather, title companies, escrow companies, attorneys and other providers of 1100-series settlement services would likely be forced to market their services almost exclusively to lenders, who will be the predominant or sole sources of GMPAs.

Major lenders will, of course, be aware that inclusion in the GMPs developed by them may be the only effective means by which providers of title and closing services will be able to obtain any significant amount of business in residential mortgage loan transactions – or, indeed, to survive. Moreover, HUD has structured its GMPA proposal in a way that mortgage lenders are in a position to realize greater profits on their GMP prices by negotiating lower prices from the providers of the services in the package. The combination of these two factors means that providers of title/closing services will face enormous economic pressure to offer cut-rate prices and/or cut-rate services in order to be selected for inclusion in lender-created GMPs. (As will be discussed in Part IV, below, provisions of state insurance law may inhibit or limit the ability of title companies to offer discounts on regulated charges to major lenders.)

It is important to note that the discounts or other things of value providers of title and closing services may be forced to offer to major lenders in order to be included in their packages will not simply reflect cost savings realized by the title company in having one or relatively few lender customers, rather than hundreds or thousands of individual consumer customers.[20] Rather, such payments and discounts will reflect a form of tribute or toll that may have to be offered to lenders as the price that has to be paid in order to have access to the ultimate customers or to have a chance for economic survival.

While HUD may believe that such loss of revenues for the title/closing industry is desirable if consumers reap the benefits of such revenue transfers, there is no comprehensive study – indeed, no responsible study at all – that supports the conclusion that the loss of such revenues (a) will simply eliminate "fat" or unnecessary charges, or (b) will not adversely affect the ability of the industry to continue to provide needed services, or to retain and attract capital.[21]

Finally, we believe that HUD's GMPA proposal would provide an artificial competitive advantage to the country's biggest lenders over their smaller competitors, and would further increase concentration in the mortgage lending industry. In recent years, the concentration trend in the mortgage lending industry has been pronounced. For example, in the last five years, the market share of the top 10 originators of residential

[20] Indeed, other than some potential savings in marketing costs and modest operational efficiencies, there are no significant savings in the title-related or closing-related work that has to be performed in 100 transactions involving 100 different properties whether those transactions involve a single mortgage lender or multiple lenders.

[21] Moreover, we doubt that competition among mortgage lenders in all markets, for all classes of customers, and for all loan products will always ensure that any lower prices for third-party services negotiated by a particular lender, or other payments or things of value that the lender may obtain for selecting a provider for its packages, will be passed along to the consumer.

mortgages has doubled from 25% of the market to "control of upward of 50%."[22] HUD's GMPA proposal would enable major lenders to achieve an even greater cost advantage over their smaller competitors by enabling them to obtain and retain price discounts or referral fees from third-party providers of services to buyers and seller of real estate that smaller lenders may not be able to obtain. This is an artificial advantage in the sense that it does not reflect any inherent cost efficiency that large lenders have over small lenders in their loan origination activities. Rather, it reflects only the green light that would be provided by HUD to large lenders to use their clout to effect revenue transfers from providers of title and closing services without running afoul of RESPA § 8.

As a final matter, we would note that the policy underlying the Robinson-Patman Act, 15 U.S.C. § 13 – concern about the abuse of buying power by large purchasers of goods who, by virtue of such clout, could secure unjustified lower prices from sellers than could their smaller competitors – is relevant here. While that act applies to the sale of goods, not services, the congressional concerns and policy reflected in that act deserve consideration by HUD.

[22] "Consortium Approach Gains in Home Loans," American Banker, July 12, 2002, at 1, 10.

III. HUD'S OBJECTIVES CAN BE ACHIEVED WITHOUT THE PROBLEMS IDENTIFIED IN PART II, ABOVE, BY HAVING LENDERS PACKAGE LENDER-RELATED SERVICES AND ANYONE PACKAGE THE OTHER SETTLEMENT SERVICES.

ALTA appreciates and, indeed, supports many of the objectives that HUD is seeking to achieve through its GMPA proposal:

- creating a regime that fully serves consumer needs in both purchase transactions and refinance transactions;
- eliminating surprise charges or junk fees at closing;
- enabling consumers early on in all real estate transactions to know what the settlement costs will be; and
- allowing consumers to shop for providers on the basis of a firm quote for all lender-related charges and all other settlement charges required for the settlement of the underlying real estate transaction.

However, ALTA also believes that these objectives can be achieved <u>without</u>:

- impairing the ability of consumers in transactions involving the purchase and sale of residential real estate to select providers of title and closing-related services of their own choosing that meet their needs;
- placing lenders in the effective position of controlling the market access of providers of title and closing-related services to consumers, thereby dramatically eliminating market outlets for these settlement service providers and potentially foreclosing all market access for smaller providers who are unable to get into the packages of significant mortgage lenders;
- enabling lenders to (i) profit from the mark-up of third-party charges at the expense of consumers or from kickbacks that such providers may have to offer to lenders in order to ensure continued access to the market, or (ii) require the use of their affiliated title companies, thereby foreclosing competitive opportunities to independent companies; and
- relying exclusively on competitive forces to ensure that discounts in prices from title and settlement service providers are passed through to consumers.

Accordingly, ALTA urges HUD to consider an alternative packaging approach that would involve two types of packages:

- **"Guaranteed Mortgage Packages" (GMPs)** that would be offered by lenders along the lines of the current HUD proposal (or as it may be modified after the public comment period) and that would consist of: (i) a loan at a guaranteed interest rate in accordance with whatever requirements HUD ultimately determines is appropriate; and (ii) all lender-related services and charges (basically the 800 series charges on the HUD-1 form); and

- **"Guaranteed Settlement Packages" (GSPs)** that could be offered by any party – title insurers and title insurance agents (including title companies affiliated with lenders), real estate brokers, lenders, escrow companies, or attorneys – and that would provide a guaranteed single price for all of the 1100 series services and charges (the title and related charges), the 1200 series charges (government recording and transfer charges), and those charges required for title assurance or closing purposes that may be listed in the 1300 series (miscellaneous settlement charges).

This "two-package" approach would achieve HUD's goal of (1) ensuring price certainty in the settlement process for consumers, and (2) injecting significant, "shoppable" price competition into both the lending and the settlement industries. It would also serve other important goals, such as allowing settlement providers to market directly to consumers, rather than relying on referrals from lenders and other parties, and preserving the competitive access of the diverse and vibrant small businesses that make up a significant part of the American settlement industry, without the potential dislocations and negative economic impact that is threatened by the HUD proposal.

Finally, in addition to achieving these macro-economic goals, GSPs could be readily tailored to accommodate the many variations in real estate practices around the country for purchase transactions and for refinance transactions, all in the context of a meaningful, guaranteed price that the consumer could readily shop. For example, in those markets where it is customary for the seller to pay for an owner's title insurance policy in support of the seller's title-related covenants in the deed of transfer, a GSP would include an owner's title policy.

The services and charges that would be included in the GSP are:

- all the 1100 series charges relevant to the type of transaction and particular market involved, including:
  - all title search and examination fees (including abstract fees);
  - owner's and loan title insurance policies;[23]
  - charges for the handling of the settlement/closing (including all incidental internal or third-party charges or expenses that the title company or settlement agent may have to incur in the handling of the settlement/closing, such as wire transfer charges and express delivery charges);
  - fees for the preparation of documents not related to the loan (*e.g.*, the deed);
  - notary fees;
  - Torrens registration fees; and
  - the buyer's attorney's fees in areas where such fees are customary;[24]

[23] In areas where owner's title insurance policies are optional, GSP packagers might offer either two GSPs (one with, and one without, the owner's policy) or one GSP that included the owner's policy, with a credit for a specified amount if the buyer elected not to purchase the owner's policy. The GSP offer would make clear that additional coverages that may be requested by the buyer in the form of endorsements may involve additional charges.

[24] Fees for the lender's attorney (in those parts of the country where such charges are paid by the borrower) would be includable in the lender GMP. Any fee for the seller's attorney (if the seller retains an attorney) would not be included in either the GMP or the GSP.

- all 1200 series recording fees, transfer taxes, and other governmental charges;[25] and
- those 1300 series charges required for the title assurance (*e.g.*, survey).[26]

While it is impractical for anyone other than a lender to offer a GMP (which must include the offer of a loan), any party could offer a GSP, although it is likely that title companies, real estate brokers, lenders, escrow companies, and attorneys will be the primary persons offering such packages. Title companies affiliated with lenders could, of course, offer GSPs in competition with independent companies, but would have no unfair competitive advantage because, as discussed below, RESPA § 8 would, in general, continue to apply to the GSP regime, so that a lender could not require the use of an affiliated title company to provide the GSP.

In general, ALTA believes that there does not need to be a wholesale exemption from RESPA § 8 for payments within, or the prices of, GSPs. As a consequence of the fact that firm pricing would be offered in the GSP in advance of settlement, ALTA believes that the following clarifications of, or exemptions from, RESPA § 8 would be necessary:

[25] It makes sense for the GSP to include these governmental charges because title companies and other GSP packagers are better able to determine the amounts of these charges in any particular locale and would likely be called upon to provide – and stand behind – such information if the charges were included in the lenders' GMPs.

[26] Generally, the 1300 series is used for those buyer-requested services that are not required by the lender or by the title company (*e.g.*, structural inspections, home owner warranty insurance, radon or lead-based paint inspections). Because the GSP offer would disclose all of the services included in the GSP price, it would be clear that such buyer-requested services would not be included.

- discounts offered by third-party providers for services in the GSP would be permitted but such discounted prices could not intentionally be "marked-up" in calculating the package price (as in HUD's proposed new GFE regime); this will ensure that such discounts will benefit consumers in GSPs, rather than simply relying on competition to ensure that any such discounts are passed through to consumers (as is the case with HUD's current GMPA proposal);

- in developing the GSP guaranteed price, there would be no § 8 violation in the use of an "average" charge for third-party services or charges included in the package, even if the actual charge incurred by the packager in the particular transaction was lower than the "average" charge used to price the GSP;[27] and

- GSP packagers should be allowed to require the use of affiliated providers.[28]

While the GSP would have to be offered at a single, guaranteed price, all of the specific services or governmental charges included in the package would be identified as part of the GSP offer. The offering of the GSP at a single, guaranteed price ensures that consumers will have a single, easy to understand figure, in order to shop among various providers of GSPs. The identification of the services contained in the GSP will enable the consumer (or her representative – her real estate agent or attorney) to ensure that any GSP offered, including those offered at very low prices, will contain all of the specific

[27] While ALTA believes that such "average" pricing is not currently a violation of RESPA § 8, such clarification is needed in light of HUD's view that such pricing may be a RESPA violation.

[28] Because consumers will be shopping among a wide variety of parties who will be offering GSPs, including companies who will be using affiliates to provide the various services to be contained in the GSPs, it makes no sense to constrain the ability of a packager to use the services of an affiliate in its GSP. Moreover, while independent providers are understandably concerned about lenders or other controllers of business requiring the use of their affiliates under the current RESPA regime (where the independent company cannot provide a financial inducement to induce the controller of business use its services), that concern would not exist in a world of GSPs because independent companies would have the ability to offer their GSPs to consumers in competition with the GSPs offered by lenders or others.

services that the consumer needs or wants, and the appropriate governmental charges that will have to be paid in the transaction. Unlike HUD's proposed GMPA regime, this will ensure that consumers can meaningfully compare GSPs offered by different providers on an apples-to-apples basis.

We believe that it might be useful for the GSP offer to identify the total amount of government charges included in the GSP price, so as to ensure that the government charges – which should not vary from one provider's GSP to another – are correctly reflected in the GSP price, thereby enabling consumers to compare the prices of the services contained in two GSP packages.[29] GSPs offered in areas where it is customary for the seller to pay for all or a portion of particular services (such as the handling of the closing, or the owner's title insurance premium) could continue to facilitate such seller pay practices through information provided to the parties.

Any additional charges to be paid by the buyer as a result of additional services or options selected by the buyer (such as an endorsement to the owner's policy to cover special risks not normally covered by the owner's title insurance policy) would have to be based on an agreement by the consumer requesting the service, and would be outside the GSP price. This would allow the continuation of current, valuable real estate practices whereby owner's (and lender's) policies of title insurance are tailored, through specific additional policy endorsements, to meet the parties' needs.

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[29] Such disclosure will also help consumers understand the extent to which governmental charges affect the total amounts they must pay at settlement.

The alternative proposed by ALTA would ensure that, in both purchase and refinance transactions, consumers would be able to shop effectively for competing GSP packages separately from their shopping for GMPs from mortgage lenders. This would inject significantly greater competition into the market for settlement services than would be the case under the current HUD proposal, where lenders are likely to be the only packagers of GMPAs. Moreover, the two-package approach would better ensure that consumers have an opportunity to select the best provider of the mortgage loan and the best provider of the settlement service package since there will be separate competition for the two packages and consumers will be able (if they want) to shop for the GSP at the time relevant to selecting the settlement service provider rather than the lender.

We believe that packagers of GSPs should, either immediately upon request or within one or two business days, be able to provide the consumer with a written guaranteed GSP price for any transaction based on information provided about the location of the property, the purchase price of the house, and the amount of the mortgage. Accordingly, there would be no need to link the timing of the offering of GSPs to the timing of the offering of GMPs (*i.e.,* within three business days of receiving a loan application). This would allow separate and real competition to develop for the GSP at a time when the consumer is ready to shop for those services. It would also allow competition to develop that would cater to specific customer desires on the balance between service, convenience, and price. Such non-price factors, which are important to buyers and sellers in many markets, are ignored by HUD's proposal, which takes into account only the lender's balance of these factors. In addition, GSPs, because they are not dependent on interest rates, could be held open at the guaranteed price for at least 90 days (or possibly longer).

Finally, we believe that the packaging authorization legislation should include appropriate and reasonable enforcement provisions to ensure that GSP packagers fulfill their obligations with regard to honoring the GSP price.

In sum, we believe there are many advantages to the approach of having loans and loan-related packages separate from packages of the non-loan settlement services. Such an approach will better ensure that there is robust competition among parties who are in the best position to develop and offer the different kinds of services.

IV. COMMENTS ON OTHER PROVISIONS OF THE PROPOSED REGULATIONS.

This Part presents ALTA's comments on other provisions or issues raised by the proposed regulations and on a number of the issues on which specific comments were invited.

A. Comments On The GFE Proposal.

1. What charges are includable in Category III(D) ("Title Services and Title Insurance")?

The proposed revised GFE form identifies as a separate category (Category III(D)) "Title Services and Title Insurance (1100)." The "1100" refers to the 1100 series of charges on the HUD-1 form. The proposed regulations state that "[l]oan originators shall subtotal all fees or charges for title and settlement agent services and title insurance in this category of the form."[30] While the proposed regulations are not entirely clear in this regard, it appears that HUD expects the amount listed for Category III(D) to include not only charges by title insurance companies, title insurance agencies, and other settlement agents (*e.g.*, charges for the title search, abstract, title examination, loan title insurance binder, loan title insurance policy, and settlement or closing fee), but all charges that would otherwise be included in the 1100 series of the HUD-1 form.

Based on the text of the current HUD-1 form and HUD's current instructions for completing this section of the form,[31] the other charges that might have to be part of the Category III(D) estimate include:

- document preparation fee,
- notary fee,
- attorney's fee (including any charges to be paid by the borrower for the fees of an attorney representing the lender and the seller, as well as the borrower), and
- fees charged by a private tax service, by a county tax collector for a tax certificate, or a fee to a public registrar for a Torrens certificate.

In short, it appears that the phrase "Title Services and Title Insurance" refers not only to charges made and kept by title agents and insurers, but is really a short-hand reference to all of the charges that are shown in the 1100 series on the HUD-1 form. If

[30] Proposed New Appendix C to the Regulations: "Instructions for Completing Good Faith Estimate; Sample Good Faith Estimates," Specific Instruction III(D), 67 Fed. Reg. at 49162.

[31] Appendix A to 24 C.F.R. Part 3500.

this is what HUD intends, it should make clear all of the charges that are to be included in the Category III(D) estimate.

The fact that certain charges (such as a charge by an attorney representing the buyer or the seller) are normally included in the 1100 series on the HUD-1 form but are not services required by the lender raises the question whether estimates for those charges should be included in the Category III(D) estimate. Because such charges may not be incurred in every transaction (even in an area where it may be customary for the buyer or seller to retain the services of an attorney), HUD has to decide whether:

- to require all GFE's in that area to include charges for the buyer's and seller's attorney within the Category III(D) estimate (so as to ensure that the III(D) estimate includes all 1100 series charges), or

- to leave it up to each lender to determine whether to include such charges in their Category III(D) estimate – in which case HUD should require lenders to disclose whether their estimates include these attorneys' charges so that consumers can compare III(D) estimates by different lenders on an apples-to-apples basis when some lenders will include those fees and others will not – or

- to specify that any service or charge separately agreed to by the buyer or the seller (such as their attorney's services) need not be included in the Category III(D) estimate – a solution that makes the most sense, but would mean that the GFE will not cover all costs incurred by the parties in the transaction.

2. What is the tolerance for such estimates: what does "lender selected" or "borrower selected" mean?

Category III(D) on the new GFE form contains two lines, one of which must be checked off by the lender, indicating either "(1) __ lender selected" or "(2) __ borrower selected." It is not clear whether "lender selected" and "borrower selected" means (i) the provider of the services whose charges are included in the Category III(D) total have been selected by the lender (or the borrower), or (ii) the services have been selected by the lender (or the borrower), or (iii) both the services and the provider have been selected by the lender (or the borrower). Neither the footnotes to the GFE form, nor the proposed regulations, nor the explanation of the proposed regulations provide a conclusive answer to this question.

A footnote to the new GFE form states that "the charges listed in . . . D (if selected by the lender) will not vary . . ." and that "the charges listed in D (if selected by the borrower) . . . must not be exceeded at settlement by more than 10% . . . except where a borrower chooses to purchase a more expensive service." But lenders and consumers do not select "charges," they select either "services" or "providers" or both.

The instructions for completing the Category III(D) section of the GFE are likewise ambiguous. The second and third sentences of the instruction states that "the loan originator also must indicate whether the services and insurance are loan originator selected or borrower selected," and that if the services are loan originator selected, there is a 0% tolerance. This language suggests that the "lender box" should be checked off if the service is one chosen by the lender.[32] However, the next sentence in the instructions states that if "title services and/or insurance are shoppable by the borrower," and the borrower ends up selecting a provider identified by the lender, then there is a 10% tolerance on the estimate. This sentence suggests that whether the lender box or the borrower box should be checked off is a function of who selects the provider.

[32] 67 Fed. Reg. at 49162.

Assuming the box to be checked and the determination of whether a 0% or 10% tolerance applies is a function of who selects the provider, there is a further problem deriving from the fact that, in a transaction involving the sale of property (and not just a mortgage loan), the 1100 series – and hence the single, total figure HUD expects lenders to put down for Category III(D) charges – includes a range of services and charges by providers who may have been selected by different parties, including the lender, the buyer, and the seller. HUD's approach appears to assume that all of the charges included in Category III(D) would be provided by a single entity selected by either the lender (0% tolerance), by the borrower based on a recommendation by the lender (10% tolerance), or by the borrower on her own (no tolerance limit). Since the new GFE does not have a separate breakout for each of the 1100 series services, it is not clear what tolerance applies if some providers of services are chosen by the seller and the buyer (*e.g.*, an escrow company), some by the lender, and some by the borrower.

3. The need for the disclosure of more information about the services included in the Category III(D) charge.

The fact that the lender does not need to disclose what services are or are not included in Category III(D) creates a significant problem for consumers who seek to shop for Category III(D) services – something HUD wants to encourage. For example, having gotten an estimate for Category III(D) services of $500 from Lender A and an estimate of $750 from Lender B, the consumer will not know:

- what services have been included in the two estimates so as to be able to make an apples-to-apples comparison;

- whether Lender B may have included in Category III(D) some services or charges that Lender A does not require;
- whether the failure of Lender A to include those services may result in the consumer having to separately purchase those services if she believes they are needed to protect her interests; and
- whether Lender A has listed some charges in other categories that Lender B is including in Category III(D).

In short, getting two different Category III(D) prices from two different lenders without knowing all of the services and charges included in those prices does not really help the consumer select the "lowest cost" lender.

The third bullet immediately above demonstrates a significant problem for consumers. While HUD wants to avoid having the GFE provide more detailed information on the nature or amount of the particular services included by a lender in its Category III(D) estimate, in transactions involving a sale of property more information has to be provided to the borrower so that (a) the borrower (and her real estate agent and/or attorney) can determine whether the services the lender is including in the III(D) total that will meet the lender's needs for the loan transaction are sufficient to meet the buyer's needs in the sale/purchase transaction, and (b) to avoid confusion and problems at settlement if, as may well be the case, the buyer/borrower has agreed to purchase other series 1100 services beyond those that are needed by the lender and covered by the lender's estimate.[33]

[33] The new GFE form contemplates that the only "optional" service that a borrower (buyer) may elect to purchase beyond the services included in the lender's Category III(D) total is owner's title insurance. In many parts of the country, this is not an optional item in a real estate transaction.

4. The treatment of title insurance agent charges and the title insurance premium in Attachment A-1 to the GFE.

In an effort to keep the GFE to a two-page document, HUD is proposing an Attachment A-1 to the GFE that will disclose some additional information that HUD believes is relevant to consumer shopping or required by existing RESPA provisions. Section B of Attachment A-1 proposes to require the lender to disclose "the subtotals of all the charges for title and settlement agent services, <u>including any commissions for title insurance</u>; and the subtotal for the title insurance premium."[34] The Instructions for Attachment A-1 add little to this language, stating only that "in reporting subtotals for mortgage broker/lender and title agent/title insurance, the loan originator must indicate the names of the service providers and the subtotals of all their charges and fees."[35] The Supplementary Information contains the following explanation:

> In a similar vein, Attachment A-1 also breaks out title agent services and title insurance into separate subtotals for the actual title insurance versus compensation to the title agent. Title agents routinely receive direct payments from borrowers for their services as well as commissions from the insurance premium for the sale of insurance. The title agent subtotal will add up these costs so that the borrower can compare, and possibly negotiate, these charges.[36]

The proposal that the title insurance agent disclose the commission it receives for the issuance of the title insurance policy appears to have its roots in an earlier HUD

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[34] Attachment A-1, 67 Fed. Reg. at 49166 (emphasis added).

[35] In fact, there is no space on the proposed Attachment A-1 form for the names of the title insurance agent or insurance company.

[36] 67 Fed. Reg. at 49149.

opinion expressed in a February 25, 2000 letter to the Massachusetts Bankers Association in which HUD stated that, in its view, the current instructions for the completion of the HUD-1 form requires that title insurance commissions received by settlement agents and closing attorneys be separately shown on the form. As ALTA has previously communicated to the Department, we do not believe that the authority relied upon by HUD for this conclusion supports the conclusion.[37] For the same reasons as expressed in that letter, we do not believe that HUD has the authority to require disclosure of such confidential business information in the revised GFE form.

Moreover, a number of questions are raised by the direction in Attachment A-1 that the amount of the agent's commission be included in the subtotal for "Title Agent Charges." These include:

- whose commissions and charges should be included in the Attachment A-1 form;
- whether the amount of the commission that would have to be included in the disclosure is the commission realized only in connection with the issuance of the loan policy or the commission realized in connection with the owner's policy as well (which might or might not be issued in the transaction); and
- whether the amount of the title insurance premium that would be reported should reflect the total premium (in which case, the amount of the agent's commission would be double counted in the two subtotals) or only the net premium remitted to the insurer.

[37] For the Department's convenience, a copy of the June 15, 2000 letter from ALTA to HUD Assistant General Counsel Kenneth Markison is attached to these comments as Appendix A.

B. Comments On The GMPA Proposal.

1. The need for disclosure of the title and closing-related services contained in the GMPA.

HUD's proposal "does not require packagers to itemize the services included in the GMPA."[38] HUD does not explain why the services contained in the package do not have to be disclosed, although, in a footnote, it refers to the considerations on this issue that were discussed in the 1998 HUD/Federal Reserve Board report, which concluded that such disclosure was not necessary.[39] However, in completing the HUD-1 form in transactions involving a GMPA, all the services of third party providers included in the package must be noted as included in the GMP price listed as the origination fee on line 801, but no separate price is to be shown for any of those particular services.

As discussed in Part II.A., above, consumers in purchase transactions need to know both (a) what title-related services are included in the GMPA so as to determine whether such services will protect their interests, and (b) the amount of the GMP price attributable to those services so as to be able to avoid paying twice for services they have elected to obtain outside the GMPA or to determine the amount of the seller's contribution to the buyer's closing costs in areas where it is customary for the seller to pay for certain title-related and/or closing costs.

[38] 67 Fed. Reg. at 49153.

[39] *Id.* at 49144, n.30, which indicates that there was a concern that itemization might lead some packagers to create longer lists that could confuse borrowers and hinder their shopping, and that lenders had pointed out that "services are performed in large measure to protect their security and when the initial disclosure is provided they may not know what is needed in each case."

The HUD proposal also calls for an Attachment A-1 to the GMPA on which the lender is to indicate whether it anticipates that certain specified services will be included in the guaranteed package.[40] The specified services are: pest inspection, lender's title insurance, property appraisal, and credit report. There appear to be two reasons why HUD is requiring lenders to identify whether the GMP is expected to include these four services.

First, HUD indicates that it is useful for the borrower to have this information because these services are of "specific interest and value to the borrower," and "some lenders may choose to forego some or all of these services."[41] Presumably, if the borrower is told that the lender is not obtaining a pest inspection or appraisal, the borrower may decide to purchase these services herself, particularly in a purchase/sale transaction. With regard to loan title insurance, HUD suggests that whether or not the lender is obtaining such insurance "may affect the cost of owner's title insurance."[42]

Second, Attachment A-1 also specifies that, upon request, the borrower is "entitled to receive a copy of the reports generated . . . ." Accordingly, a second HUD rationale for the Attachment A-1 list appears to be to ensure that if the GMP price to be paid by the

[40] 67 Fed. Reg. at 49170.

[41] *Id.* at 49153.

[42] *Id.* As noted above, in many parts of the country where both a loan and owner's policy are issued, the basic price for title insurance is determined by the charge for the owner's title insurance policy, with the cost of the loan policy, when issued simultaneously with the owner's policy, being an "add-on" charge that is quite low and generally a fixed dollar amount ($50 to $100 in most jurisdictions).

borrower includes any of these four services – all of which result in a written report or document – the borrower will get a copy of what she has paid for.

While providing the consumer with a copy of the pest inspection, property appraisal, and credit report obtained by the lender may avoid the consumer's need to obtain those services and reports on her own, this is not the case with the loan title insurance policy. Providing a copy of that policy to the consumer in no way protects the consumer or is a substitute for the consumer's obtaining a title insurance policy covering her separate interest in the property.[43] Accordingly, HUD may be misleading the consumer into believing otherwise by including the loan title insurance policy in the Attachment A-1 to the GMPA and we recommend that reference to the loan title insurance policy be deleted from the Attachment.

2. Issues relating to the wholesale exemption from § 8 being proposed for the GMPA.

To induce lenders to offer GMPAs, HUD is proposing a wholesale exemption from § 8 for the pricing of the GMP package and for all services provided within the GMPA. Indeed, the "carrot" of the safe harbor is not only a significant inducement, but the consequences of losing the safe harbor – and thereby being exposed to sanctions for violations of § 8 because of various actions taken in connection with the GMPA – is also the only "stick" HUD can use (given the lack of statutory authorization) for ensuring that lenders comply with the various proposed GMPA requirements.

[43] Indeed, a number of states require that the buyer be informed that the loan policy will not protect the consumer's interest. *See, e.g.*, Ala. Code § 27-25-7; Mo. Rev. Stat. 381.015.

ALTA believes that there are serious legal constraints on HUD's authority to override existing statutory requirements through the mechanism of such exemptions. These constraints were discussed in a memorandum submitted by ALTA to HUD on April 8, 2002, a copy of which is attached as Appendix B to these comments. Moreover, as discussed in Part II.A., above, we believe that parties who might otherwise be involved in developing and participating in packages will be reluctant to do so in the face of the § 8 lawsuits and liabilities they would face if the packager failed to comply with one of the HUD GMPA requirements and the § 8 safe harbor were therefore lost.

C. Responses To Particular Issues Raised By HUD.

1. **Question 6 (Greater Itemization in the GFE):** ***In Section III.B.(1) b., the proposed rule simplifies the GFE by placing all loan origination costs in a small number of primary categories. This is intended to facilitate borrower understanding and shopping of major loan costs and minimize the proliferation of "junk fees" and duplicative charges. How could the GFE be made even simpler to facilitate borrower shopping? If the commenter believes greater itemization is desirable, what should be itemized and why?***

As discussed above, ALTA believes that, at least with regard to Category III(D), greater itemization is required in order to enable the consumer to do an apples-to-apples comparison between Category III(D) estimates, to ascertain whether title and closing-related services that will meet her needs are included in the estimate, and to determine whether she can obtain the services she wants or needs for her own interests at a better price than is being offered by the lender.

2. **Question 11 (The Need for a § 8 Safe Harbor).** ***Is a safe harbor along the lines proposed in Section III. C. (1) of this rule necessary to allow lump sum packages of settlement services to become available to borrowers? Would the proposed clarification by HUD that discounts may be arranged, if passed on to borrowers and not marked up, suffice to make packages available to borrowers? Would a rule change to approve volume discounts and/or mark-ups when a package is involved suffice? Would it suffice to trim the disclosure requirements for packaging and offer the option of providing a streamlined GFE to those who packaged?***

As evidenced by ALTA's proposed GSP regime discussed in Part III, above, which we believe can operate without a wholesale exemption from § 8, ALTA does not believe that a safe harbor along the lines proposed in III.C.1. of the rule is necessary to allow for consumer-oriented packaging. In particular, ALTA believes that any discounts negotiated by the packager in the charges of third-party providers should be passed through to the consumer in the package price. However, as discussed in Part III, certain modifications to HUD's position on "averaging" (*i.e.*, where a title or settlement company at closing may have to use an average of the likely charges by third parties because the exact amount, or whether the service will be used at all, may not be known at that time) need to be made.

3. **Question 12 (Application of the Safe Harbor to Referrals to the Packager).** ***As proposed in Section III. C. (6) is the scope of the safe harbor appropriately bounded in applying to all packagers and participants in packages? The safe harbor also currently does not apply to referrals to the package. Should there also be a bar against part time employees of other providers working for the package to steer business? How should the safe harbor apply to affiliated business arrangements to protect borrowers from steering?***

ALTA does not believe that there should be an exemption from § 8 for referral fees or other payments given to persons for the referral of the consumer to a particular package. Such payments will tend to inflate the costs of packagers and could skew the recommendations of parties who would otherwise provide advice to the consumer on the selection of a package. Indeed, whatever rules are applied to referrals and payments outside the packaging context should be applied to payments for the referral of business to the packager (whether to part time employees or other settlement service providers).

With regard to affiliated business arrangements, lenders who use such affiliates in connection with the provision of title and closing-related services in connection with their GMPs should continue to be subject to the safe harbor requirements for affiliated business arrangements – particularly the "no required use" requirement – so as to ensure that settlement service providers not affiliated with the lender are not foreclosed from market access. [44]

[44] There is no inconsistency between ALTA's position that lenders who provide GMPAs should not be allowed to require the use of affiliated providers in their packages and ALTA's view that such limitation is not required with regard to the GSPs under ALTA's proposal. (*See* p. 33, above.) Under the GMPA proposal, lenders may be the only viable packagers and an exemption from § 8 that would allow lenders to require the use of affiliated providers will foreclose many providers of settlement services who are not affiliated with lenders from access to the market. Under ALTA's GSP proposal, however, these providers would be able to offer their own packages or join in the packages of others, and lenders would have no inherent ability to deny them access to the market. Moreover, companies that will offer GSPs are likely to use their affiliates to provide services in the packages they offer.

Accordingly, the "no required use" safe harbor is needed in the GMPA context to ensure that providers not affiliated with lenders have an opportunity to compete for the consumers business, whereas such protection is not needed in the GSP context where all providers of title and closing services have a reasonable opportunity to offer, or be part of, GSPs.

We also believe that the safe harbor requirement regarding disclosure of the existence of the affiliated business arrangement should continue to apply with respect to title and closing services. Buyer/borrowers may not care whether an affiliated entity provides a credit report, flood certification report, or other lender-needed service in order to make the mortgage loan, and will not base their decision on the selection of a lender because of such affiliated business arrangements. But with regard to the provision of title and closing services, knowing that the lender may be using an affiliated business to provide those services may be a relevant piece of information for the buyer and seller (and their advisors, such as the real estate agent or attorney) in shopping for a GMPA and in deciding whether to enter into a GMPA with one lender rather than another.

4. **Question 22 (Should Inconsistent State Laws Be Preempted?).** ***To what extent, if any, do inconsistencies currently exist, or would they exist upon promulgation of the proposed rule between State laws and RESPA? Specifically, what types of State laws result in such inconsistencies and merit preemption? What, if any, provisions of the proposal should be revised to facilitate any necessary preemption?***

This is a most important question from the standpoint of the title insurance industry since title insurance and related charges are regulated under state law and, in some states, extensively regulated. The first part of this answer discusses the kinds of state law provisions that are likely to apply to the offering of discounts, referral fees or other forms of consideration by regulated title companies even in the face of a HUD exemption for such payments from RESPA § 8. The second part discusses the reasons why ALTA believes that HUD cannot and should not preempt such state laws.

a. State law provisions that are relevant to the pricing of services in a package and to lender requirements that particular providers be used.

There are a number of state law provisions that would apply to discounts or payments by title insurance companies and agents in order to become part of a lender's package. For example, several states have enacted provisions similar to RESPA § 8 that broadly prohibit kickbacks and referral fees in the provision of settlement services in residential real estate transactions.[45] Almost all states have statutory measures that prohibit the giving of any rebate or inducement by an insurer or insurance agent to a lender or consumer in order to induce the placement of business.[46] In a number of these states, such provisions are specifically addressed to title insurance and related services provided by title insurers and agents.[47]

Similarly, a large number of states have prohibitions on a lender requiring a borrower to use a particular provider of insurance as a condition to making a mortgage loan.[48] Such provisions may prevent lenders from offering a single package price

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[45] *See, e.g.,* Md. Code Ann., art. 27, § 465 (prohibiting any person having any connection with the settlement of real estate transactions from providing a thing of value or other consideration for the purpose of obtaining or retaining any settlement service business); Va. Code § 6.1-2.13:1 (prohibiting any real estate agent, attorney, settlement agent, or lender from paying or receiving, directly or indirectly, any thing of value or other payment pursuant to any agreement or understanding that settlement service business shall be referred to any person).

[46] *See, e.g.,* Ariz. Rev. Stat. § 20-1585; Colo. Rev. Stat. 10-11-108.

[47] *See, e.g.*, Cal. Ins. Code § 12404; New York Ins. Code §6409(d); Tex. Ins. Code Ann. § 9.30. Some states also clearly prohibit the receipt of such inducements. See, e.g., Minn. Stat. Ann. §72A.08, subd. 2.

[48] *See, e.g.,* Cal. Ins. Code § 770; Conn. Gen. Stat. Ann. § 38a-816; Fla. Stat. Ann. §626.9551; Ill. Comp. Stat. Ann. ch. 205, § 5/48.2; Mich. Comp. Laws Ann. § 500.2077; N.J. Stat. §17:46B-30.1; N.Y. Ins. Law § 2502; and Ore. Rev. Stat. § 746.180. In some states, the

without providing information about the party to provide the insurance and the amount to be paid for the title insurance so that the buyer is able to select a different entity to provide the insurance.[49]

Finally, a number of states have standards governing title insurance charges that require that such charges may not be "unfairly discriminatory."[50] The purpose of this standard is to ensure that similar risks pay similar title insurance charges and that one applicant for insurance does not pay a lower insurance premium than another applicant with a similar insurance risk. In states with such standards, title insurance companies may not be able to file or use title insurance rates that are lower for insurance transactions arising from being included in the package of one lender (a large lender with clout) rather than another (with less clout). The reasons for this are obvious. From an insurance standpoint, there is no reason why Applicant X seeking to insure a transaction involving Blackacre should pay a different amount for title insurance if she obtains her policy (or pays for a loan policy for the lender's protection) in connection with a package developed by a large lender or a package developed by a small lender. Alternatively, there is no

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prohibition on a mortgage lender designating a provider extends beyond insurance to include the attorney or the entity to handle the closing (*e.g.*, Md. Code Ann. Com. Law § 12-120(c); Minn. Stat. Ann. §507.45, Subd. 4; and Va. Code § 6.1-330.70 (lender may not require the use of a particular attorney, surveyor, or insurer)).

[49] It should also be noted that some states require that lenders provide borrowers at the time of closing with a detailed statement of each charge for a settlement service that the borrower is obligated to pay. *See, e.g.,* Kan. Stat. Ann. § 17-5514; Mich. Comp. Laws. Ann. § 438.31b.

[50] *See, e.g.*, Ariz. Rev. Stat. § 20-431; Cal. Ins. Code § 12401.3; Mich. Comp. Laws §§ 500.2400, 500.7312; N.J.S.A. 17:46B-41; N.Y. Ins. Law § 6409(b); Va. Code Ann. § 38.2-4608(A).

reason why Applicant X should pay a lower price for title insurance in connection with a transaction involving Blackacre than her next door neighbor must pay in connection with an identically valued transaction involving Whiteacre.

b. Why HUD cannot and should not preempt these state laws.

Even if HUD were able to exempt discounts, payments and other things of value between settlement service providers and lenders/packagers from the prohibitions of RESPA § 8, the state law provisions discussed above would still be applicable to such discounts and payments. Moreover, the state law prohibitions on lenders requiring the use of a particular insurer would likewise inhibit a lender from requiring the borrower to use the insurer it had selected for inclusion in its guaranteed package. None of these provisions may be preempted by the Secretary pursuant to § 18 of RESPA, 12 U.S.C. § 2616, in connection with the proposed HUD regulations.

Section 18 provides that RESPA does not annul, alter or affect any person from complying with state laws on settlement practices "except to the extent that those laws are inconsistent with any provisions of this chapter, and then only to the extent of the inconsistency." (Emphasis added.) While the Secretary may determine when such inconsistencies exist, the Secretary may not determine that "any State law is inconsistent with any provision of this chapter" if the State law gives greater protection to the consumer.

Accordingly, the Secretary's ability to make preemption determinations under § 18 only comes into play if a provision of state law is inconsistent with a provision of RESPA as enacted by Congress. The state laws discussed are not inconsistent with

RESPA § 8 as enacted by Congress, or with any other provision of RESPA. Thus, the Secretary has no authority under § 18 to preempt state anti-kickback or anti-rebate laws, or state laws ensuring that borrowers may select insurance providers, or state laws that prohibit discrimination in insurance rates in order to facilitate a packaging regime that is not reflected in the RESPA statute.

Moreover, absent a clear direction from Congress on how it wants any federally-established packaging regime to relate to state insurance laws in this area, the Department should not arrogate to itself the resolution of such an important issue of federal-state relations. The state laws in this area are both long standing and reflect consumer protection policies in areas that have traditionally been within the purview of state law. Whether and how those state interests should be accommodated, or whether those state laws should be preempted, is a very fundamental issue that is properly to be resolved only by Congress.

* * * * *

ALTA appreciates HUD's consideration of these views. If we can provide any further information or clarification of the views expressed in these comments, please do not hesitate to contact us.

James R. Maher
Executive Vice President

cc: The Hon. Mel Martinez
The Hon. John C. Weicher
The Hon. Richard A. Hauser, Esq.
Mark A. Calabria, Deputy Assistant Secretary for Regulatory Affairs
Ivy Jackson, Acting Director - RESPA
Assistant General Counsel Kenneth A. Markison, Esq.

AMERICAN
LAND TITLE
ASSOCIATION

APPENDIX A

June 15, 2000

Kenneth A. Markison, Esq.
Assistant General Counsel
GSE/RESPA
U.S. Department of Housing and Urban Development
451 Seventh Street, S.W.
Washington, D.C. 20410

Dear Mr. Markison:

We recently became aware of a memorandum entitled "HUD's Response to Questions from the Massachusetts Bankers Association," which was sent to that association under a cover letter from you dated February 25, 2000. On page 9 of the memorandum, HUD responds to several questions relating to the disclosure of title charges on the HUD-1 form. For the reasons discussed below, we believe that the conclusion expressed in the answer to question 1 and the explanation given for that conclusion are clearly incorrect. We hope that HUD will correct this error as quickly as possible.

The question and answer were as follows:

> (1) Is it required to indicate anywhere on the HUD-1 the actual dollar amount of the commission earned by the settlement agent (closing attorney) for issuing a title insurance policy?
>
> Answer: Yes. The Instructions specifically state that the HUD-1 must "itemize all charges imposed upon the borrower and the seller by the lender and all sales commissions, whether to be paid at settlement or outside of settlement." (See Instructions) (Italics added).

Not only is the answer wrong, but the quote from the HUD-1 Instructions does not support – and, indeed, has nothing to do with – any purported requirement that the amount of any insurance commission must be separately itemized on the HUD-1 form.

To begin with, nothing in RESPA, in the regulations, or in the HUD-1 Instructions requires or suggests that any insurance commission or title agent "retention"[1] has to be separately itemized on the form. Until the memorandum to the Massachusetts Bankers Association, we have never seen a suggestion from HUD or from any other source that such itemization was required.

Indeed, there would be no reason grounded in RESPA policy for such separate disclosure.

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[1]Title insurance agents, unlike agents in other lines of insurance, do not merely "sell" insurance policies but are significantly involved in evaluating the risks, in determining insurability, and, in fact, generally issue the insurance policies on behalf of the insurer. As a consequence, they retain a portion of the one-time title insurance premium for these services and remit the net premium to the insurer. The amounts they retain are referred to in the industry as agent "retentions" rather than agent "commissions," a term that reflects the unique role they play in the policy issuing process.

It is the title insurance premium that is paid by the consumer and that amount is disclosed. Moreover, a requirement that the commissions or retentions realized by insurance agents must also be disclosed on the HUD-1 form would greatly complicate the form since such disclosures would have to be made for any homeowner's insurance policy, credit life policy, and mortgage insurance policy issued in connection with the transaction.

Second, the reference in the answer to the language in the Instructions that "all sales commissions" must be disclosed is completely irrelevant to whether "insurance commissions" must be disclosed. The language quoted in the answer is taken from the second paragraph of the General Instructions section of the Instructions, not from any of the Line Item Instructions that relate to title insurance or other insurance charges. More importantly, the phrase "sales commissions" in the General Instructions unambiguously refers to the "sales commissions charged by the sales agent or broker" that must be entered on Line 700, i.e., the commissions charged by the real estate broker or salesperson for handling the sale of the property. The phrase "sales commission" is only used in the series 700 Line items and has no relevance to the commissions paid to insurance agents.[2]

Third, nothing in the Instructions relating to the Line 1100 series – the line items that address title insurance and attorney charges – suggests such a requirement. The only remotely relevant reference to this topic is contained in the instructions to Line 1113, which specify that this line should be used "to disclose services that are covered by the commission of an attorney acting as a title agent when Line 1107 is already being used to disclose the fees and services of the attorney in representing the buyer, seller, or lender in the real estate transaction." (Emphasis added.) There is no reference to using any line in the 1100 series to disclose the amount of the title insurance agent's retention – whether the agent be an attorney or a non-attorney.

In sum, the Instructions provide no basis for the conclusion expressed in the HUD memorandum on this question. Indeed, to the best of our knowledge, HUD-1 forms are never completed in the manner suggested by the answer to question 1. We are obviously concerned that HUD's answer to this question is at odds with the universal understanding of the industry and those who complete the HUD-1 forms, and that this answer, if it became generally known, could create significant and unfortunate confusion.

Accordingly, we urge HUD to take prompt action to clarify that insurance commissions and title insurance retentions do not have to be separately disclosed on the HUD-1 forms.

If you have any questions about this letter or would like to discuss this matter, please do not hesitate to contact me.

Sincerely,

James R. Maher,

cc: Rebecca J. Holtz
Tanya M. Duncan
Massachusetts Bankers Association

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[2] As discussed in note 1, above, the term "sales commissions" has even less relevance to the retentions of title agents in light of the fact that the compensation they receive is, in significant measure, for the work performed on behalf of the insurer in the issuance of the policy.

APPENDIX B

AMERICAN
LAND TITLE
ASSOCIATION

WHY LEGISLATIVE AUTHORIT Y IS NEEDED
TO IMPLEMENT A REGIME OF
LENDER GUARANTIES OF CLOSING COSTS

American Land Title Association
April 8, 2002

INTRODUCTION AND SUMMARY

HUD has announced that it is considering the development of a regulatory regime by which mortgage lenders would provide consumers, early in the process when a consumer is shopping for a mortgage loan, with a guarantee of the total cost of a package of real estate settlement services required by the lender in connection with a federally-related mortgage loan to the consumer. To encourage lenders to provide such guarantees, HUD may be considering using its authority under §§ 8(c)(4)[1] and 19(a)[2] of the Real Estate Settlement Procedures Act (RESPA), to exempt lenders and the providers of services in the package from the anti-kickback and fee-splitting provisions of § 8 and from certain disclosure requirements under § 5.

Hundreds of thousands of businesses and individuals are involved in providing real estate settlement services throughout the nation. A major change in the way in which business is transacted, as would clearly be implicated in the widespread adoption of a lender guarantee/packaging concept, could have serious and disruptive effects on industries that facilitate millions of real estate and mortgage financing transactions each year. Such a change would constitute a very major policy decision for the federal government.

The focus of this paper is not on the wisdom, benefits, or drawbacks of such a fundamental shift in policy. Rather, it is to raise two concerns that we believe HUD

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[1] 12 U.S.C. § 2607(c)(4).

[2] 12 U.S.C. § 2617(a).

should consider in connection with any attempt to pursue such a shift through regulations issued under the existing provisions of RESPA.

First, as will be discussed in Part I below, to the extent that HUD may be contemplating the granting of exemptions from RESPA's anti-kickback and disclosure provisions in order to encourage and facilitate lender guarantees of settlement costs and packaging of settlement services, we believe there are serious legal constraints on HUD's authority to override existing statutory requirements through the mechanism of such "exemptions." Moreover, there are statutory provisions in a great number of states prohibiting referral fees, rebates and other inducements, particularly with regard to the provision of insurance and closing services, as well as state law provisions prohibiting a lender from requiring the use of a particular insurance provider, that cannot be preempted by HUD's regulatory action and that need to be considered in determining the scope of a lender guarantee/packaging regime.

Second, as discussed in Part II, below, as a matter of sound policy we believe that HUD should not embark upon a regulatory endeavor of such far-reaching implications without clear statutory authority. If the regime created by Congress in RESPA needs serious modification – so as to move away from prohibitions on kickbacks and unearned splits, and requirements for the disclosure of the costs of individual settlement services, to a regime of lender guarantees of package prices – Congress should debate and decide the statutory guidelines by which such a sea-change is to be accomplished, and the scope of the exemptions and state law preemption that may be needed to accomplish such a policy. This is too important a change to be effected by administrative action under a statutory regime that does not provide the needed guidance and structure.

I. HUD CANNOT USE ITS EXEMPTION AUTHORITY TO PERMIT LENDERS AND SETTLEMENT SERVICE PROVIDERS TO VIOLATE RESPA REQUIREMENTS.

In order to encourage lenders and settlement service providers to provide the kind of price guaranties and packaging that HUD may believe is desirable, HUD may need to exempt such parties from RESPA's anti-kickback and disclosure requirements. For the reasons discussed in this part, we believe there are serious questions as to whether HUD has the statutory authority to create the kind of exemptions that may be needed to induce the market to shift to a guarantee/packaging regime.

A. HUD Does Not Have Unlimited Authority to Create Exemptions from RESPA § 8 for Payments That Would Clearly Constitute Prohibited Referral Fees or Unearned Splits.

In order to encourage lenders to guarantee the price of a package of lender-needed services, HUD may be considering providing lenders and settlement service providers who provide services in the package an exemption from RESPA § 8 for any payments, things of value, or mark-ups that may otherwise violate that section. As discussed in this subsection, HUD's authority under RESPA § 8(c) to clarify the application of § 8 to certain payments or classes of payments does not extend so far as to give the Secretary authority to exempt payments that would otherwise be violations of § 8 in order to promote a regime that HUD may believe is better or more effective than the regime enacted by Congress.

Sections 8(a) and (b) of RESPA prohibit the payment or receipt of kickbacks, referral fees, or unearned divisions of fees. Section 8(c), as contained in the original version of RESPA enacted in 1974, provided that § 8 should not be construed as prohibiting certain kinds of payments for services actually rendered (i.e., payments to attorneys, or to title agents by title insurers for services rendered in the issuance of a policy, by a lender to its duly appointed agent for services performed in the making of a loan, and for payments of bona fide salaries or compensation or other payments for goods or facilities actually furnished or services actually performed). As the House and Senate Banking Committee reports on RESPA made clear, § 8(c) was not intended to carve out exemptions for behavior that would otherwise constitute violations of §§ 8(a) or (b), but to make explicit "the types of legitimate payments that would not be proscribed by the section."[3]

RESPA as originally enacted did not provide explicit statutory authority for HUD to promulgate regulations and interpretations for all of its provisions. Concerns were expressed that, absent such authority, HUD was constrained in issuing interpretations regarding provisions, like § 8, that were enforceable through criminal sanctions. In particular, a significant issue that arose almost immediately after RESPA became law at the end of 1974 was whether payments among real estate brokers and agents pursuant to cooperative brokerage arrangements or referral arrangements – long-standing practices in the real estate brokerage industry – might be deemed to violate § 8(a). As a consequence of this and other uncertainties created by the original language of RESPA, legislation to amend the statute was introduced in 1975 and hearings were held by the House and Senate. At those hearing, the witness for the National Association of Realtors®

[3] S. Rep. No. 93-866, at 7 (1974), 1974 U.S. Code Cong. & Admin. News 6546, 6552. Identical language appeared in the House Banking Committee Report. See H.R. Rep. No. 93-177, at 8 (1974).

discussed why such practices among real estate brokers and agents did not adversely affect consumers, explained that "[i]t is clear from the history of RESPA that neither of these practices were intended to be hit by the anti-kickback provision," and proposed an "explicit clarifying exemption" for these practices.[4]

The clarifying amendment suggested by the National Association of Realtors® was enacted as part of the Real Estate Settlement Procedures Act Amendments of 1975, Pub. L. 94-205, 89 Stat. 1158 (Jan. 2, 1976). Specifically, section 8(c) was amended to add "payments pursuant to cooperative brokerage and referral arrangements or agreements between real estate agents and brokers" to the list of payments for services rendered that Congress had previously identified in 8(c) as not being the kind of payments prohibited by § 8. Indeed, the relevant committee report explained the cooperative- brokerage amendment as "mak[ing] clear" that such payments "are not considered kickbacks."[5]

In addition to clarifying that cooperative brokerage arrangements were not the kind of payments intended to be prohibited by § 8, Congress further amended § 8(c) to provide that nothing in § 8 shall be construed as prohibiting:

> "(4) such other payments or classes of other payments or transfers as are specified in regulations prescribed by the Secretary after consultation with the Attorney General, the

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[4] *The Real Estate Settlement Procedures Act of 1974: Hearings on H.R. 5352, S.2327, and H.R. 0283 Before the Subcommittee on Housing and Community Development of the House Committee on Banking, Currency and Housing*, 94th Cong., 1st Sess., 240, 253-57 (1975) (statement of Art S. Leitch, President, National Association of Realtors®).

[5] H.R. Rep. 94-667, at 7, 1975 U.S. Code Cong. & Admin. News 2448, 2454.

> Administrator of Veterans' Affairs, the Federal Home Loan Bank Board, the Federal Deposit Insurance Corporation, the Board of Governors of the Federal Reserve System, and the Secretary of Agriculture."[6]

Although the Committee report describes this provision as giving the Secretary authority to "exempt" other classes of transactions or payments from § 8, the language of the provision, its placement in § 8(c), and normal rules of statutory construction strongly suggest that the Secretary's authority under this provision is not without limits and the exercise of that authority must be consistent with the common principle derived from the other subparagraphs that precede this grant of authority to the Secretary.[7]

The common principle that runs through the other three subparagraphs that precede § 8(c)(4) is that none of the payments or practices identified in those subparagraphs would otherwise constitute clear violations of § 8 in the absence of the clarification provided by § 8(c). This should not be surprising in light of the fact that, as

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[6] 89 Stat. 1158.

[7] As discussed below, in the 1975 RESPA amendments Congress also added § 19(a) to the Act, providing the Secretary with the authority to "prescribe such rules and regulations, to make such interpretations, and to grant such reasonable exemptions for classes of transactions, as may be necessary to achieve the purposes of this Act." Because § 8(c)(4) specifically addresses the Secretary's authority to determine when payments are not subject to RESPA § 8, it controls over the more general authority in §19(a). See, e.g., Morales v. Trans World Airlines, Inc., 504 U.S. 374, 385 (1992) ("it is a commonplace of statutory construction that the specific governs the general"); N.L.R.B. v. A-Plus Roofing, Inc., 39 F.3d 1410, 1415 (9th Cir. 1994) ("It is a well-settled canon of statutory construction that specific provisions prevail over general provisions").

Moreover, even if HUD were to consider granting an exemption from § 8 under the authority of § 19(a), such exemption would have to be "reasonable." For the reasons discussed below, granting an exemption for payments that would otherwise clearly violate § 8 in order to encourage a lender guarantee/packaging regime not authorized by Congress but believed to be desirable by the Secretary would not constitute a "reasonable" exemption.

the introductory language of § 8(c) indicates (i.e., nothing in § 8 "shall be construed as prohibiting" the payments and practices identified in the subparagraphs), Congress was not attempting in § 8(c) to exempt abusive practices from § 8 coverage. Rather, Congress was simply trying to make clear the kind of practices and payments that were never intended to be covered by § 8.

This common thread sheds light on the scope of the authority Congress conveyed in § 8(c)(4) to the Secretary to establish further clarifications of payments and transactions that were not intended to be proscribed by § 8. The fact that Congress authorized the Secretary in § 8(c)(4) to identify "such other payments or classes of payments or transfers" that would likewise not be "construed" as coming within the prohibitions of § 8 demonstrates that Congress contemplated that the Secretary's authority under this provision would be exercised in a manner consistent with the type of "clarifying" approach Congress had adopted in the previous paragraphs of subsection (c)(4).

The principle of statutory construction known as *ejusdem generis* further supports the conclusion that the "such other payments" language in § 8(c)(4) should be construed in a manner consistent with the common attribute of the other types of payments that are discussed in the preceding subparagraphs. As described in a leading treatise:

> [I]n accordance with what is commonly known as the rule of *ejusdem generis*, where in a statute general words follow a designation of particular subjects or classes of persons, the meaning of the general words will ordinarily be presumed to be, and construed as, restricted by the particular designation, and as including only things or persons of the same kind, class, character, or nature as those specifically enumerated. In accordance with the rule of *ejusdem generis*, such terms as

> "other," . . . when preceded by a specific enumeration, are commonly given a restricted meaning, and limited to articles of the same nature as those previously described.[8]

In sum, while § 8(c)(4) gives the Secretary authority to clarify when questionable payments are really not the kind that Congress intended to proscribe, that provision does not give the Secretary blanket authority to rewrite § 8 by carving out exemptions for behavior that would otherwise violate § 8. The use of such exemptions is particularly suspect where, as here, it is intended to help launch a new regulatory regime that has no legislative mandate or imprimatur.

B. HUD Does Not Have Authority to Override RESPA's Requirement That Consumers Be Given Estimates of the Costs of the Individual Settlement Services That May Be Contained in a Guaranteed Package.

As part of the incentive to lenders to encourage their moving to a regime of guaranteed prices for settlement service packages, HUD may also be considering allowing such lenders to provide consumers with only a single figure for the total price of the package without having to provide, as current law requires, estimates of the costs of the various settlement services that are contained in the package. As in the case of the requirements of § 8 discussed above, HUD should not override these disclosure requirements in order to encourage lenders to provide guarantees of packaged prices.

Section 5(c) of RESPA, 12 U.S.C. § 2604(c), provides that "[e]ach lender shall include with the booklet a good faith estimate of the amount or range of charges for specific settlement services the borrower is likely to incur in connection with the

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[8] 73 Am. Jur. 2d (Statutes) § 135.

settlement as prescribed by the Secretary." (Emphasis added.) In implementation of this statutory requirement, § 3500.7(c) of HUD's RESPA regulations provides that the good faith estimate must consist of an estimate of "each charge" listed in section L of the HUD-1or HUD1-A forms that the borrower will normally pay or incur at or before settlement. The itemization of such services is important so as to enable the consumer to understand what services may be required by the lender, what the likely charges are to be for those services, and, in certain cases, to be in a position to shop for such services.

Section 19(a) of RESPA, as added by the 1975 amendments, authorizes the Secretary to "grant such reasonable exemptions for classes of transactions, as may be necessary to achieve the purposes of [RESPA]." To the extent that the Secretary may be considering using his exemption authority under this provision to exempt lenders who offer a package of settlement services at a guaranteed total price from having to identify, and provide estimates for the costs of, the individual settlement services in the package, we submit that such an exemption would neither be "reasonable" nor "necessary" to achieve RESPA's purposes.

First, identification of the services contained in the package and the parties who will be providing those services is important to the consumer with regard to those services that will be undertaken in any significant regard for his or her benefit. Unlike a credit report or lender-required appraisal, which are obtained by the lender to assist it in making a loan and in which the buyer (i.e., the borrower) and the seller of the property will generally have no interest, the buyer and the seller have a distinct interest, separate and apart from the lender's interest, in services such as the title assurance to be provided in the transaction and the handling of the closing of the real estate transaction.

For example, in order to gain a competitive advantage by reducing its costs of title-related protection, a lender may be willing to accept a cheaper and less-comprehensive form of title protection for its mortgage loan that would be inadequate or unacceptable to the seller and the buyer for the protection of their interests.[9] To ensure that they can adequately protect their interests, buyers and sellers need to know what kinds of title-related and closing services are included in the lender's package, and the identity of the party that the lender may be contemplating to provide such services (to determine if such provider will also satisfy their needs and interests as well).[10] Moreover, in many parts of the country the seller may bear all or a significant part of such costs and, consequently, will have a significant interest in the party providing such services and the costs involved.

Second, to ensure that consumers will be able to shop for the individual services contained in the package – particularly those services that are also going to be provided for their benefit – they should continue to receive timely information on the costs of the individual services contained in the package. Moreover, such information is also necessary so as to allow the buyer to determine the amount of the credit that the buyer will get from the lender if (as we assume will be provided under any HUD proposal) the buyer and seller are free to select another provider for <u>services to be rendered for their</u>

[9] The nature of the title insurance protection provided to the buyer is important to the seller because title insurance has become the most widespread means by which sellers provide financial assurance to their buyers to back up the title warranties in their deeds.

[10] In this regard, there is a significant policy issue as to whether HUD's lender guarantee/packaging proposal will or should allow the lender to dictate to the buyer and seller the selection of the party to provide the title insurance and closing services in the transaction.

benefit that have been included in the lender's package. (As discussed in the next section, state law prohibits a lender from requiring the borrower to use a provider of insurance selected by the lender.)

In sum, providing lenders with a complete exemption from disclosing information on the individual services that may be contained in the package is neither reasonable nor would it advance the purposes of RESPA.

C. State Laws Prohibiting Referral Fees, Inducements for the Placement of Insurance and Closing Business, and Lender Designations of Insurance Providers Will Continue to Apply and Cannot Be Overriden by Determinations of the Secretary Under RESPA § 18.

Not only do RESPA requirements potentially stand in the way of achieving a lender guarantee/packaging regime through regulatory action, but certain provisions of state law may also pose a significant obstacle to such a HUD-created regime. At the very least, these provisions may pose difficulties in seeking to include insurance products, such as title insurance, in the package.

For instance, several states have enacted provisions similar to RESPA § 8 that broadly prohibit kickbacks and referral fees in the provision of settlement services in residential real estate transactions.[11] Almost all states have statutory measures that prohibit the giving of any rebate or inducement by an insurer or insurance agent to a

[11] See, e.g., Md. Code Ann., art. 27, § 465 (prohibiting any person having any connection with the settlement of real estate transactions from providing a thing of value or other consideration for the purpose of obtaining or retaining any settlement service business); Va. Code § 6.1-2.13:1 (prohibiting any real estate agent, attorney, settlement agent, or lender from paying or receiving, directly or indirectly, any thing of value or other payment pursuant to any agreement or understanding that settlement service business shall be referred to any person).

lender in order to induce the placement of business. In a number of these states, such provisions are specifically addressed to title insurance and related services provided by title insurers and agents.[12] Such provisions may inhibit the ability of title insurers and their agents to offer discounts or special deals in order to be included in the lender's package.

Similarly, the overwhelming number of states have prohibitions on a lender requiring a borrower to use a particular provider of insurance as a condition to making a mortgage loan.[13] Such provisions will prevent lenders from offering a single package price that includes such services without providing information about the party to provide the insurance, the amount that will be paid to that provider, and the credit that will be provided if the buyer selects a different person or company to provide the insurance or other service.[14]

Even if HUD were able to exempt payments and other things of value between settlement service providers and lenders/packagers from the prohibitions of RESPA § 8,

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[12] See, e.g., Cal. Ins. Code § 12404; New York Ins. Code §6409(d); Tex. Ins. Code Ann. § 9.30. Some states also clearly prohibit the receipt of such inducements. See, e.g., Minn. Stat. Ann. §72A.08, subd. 2.

[13] See, e.g., Cal. Ins. Code § 770; Conn. Gen. Stat. Ann. § 38a-816; Fla. Stat. Ann. §626.9551; Ill. Comp. Stat. Ann. ch. 205, § 5/48.2; Mich. Comp. Laws Ann. § 500.2077; NY Ins. Law § 2502; and Ore. Rev. Stat. § 746.180. In some states, the prohibition on a mortgage lender designating a provider extends beyond insurance to include the attorney or the entity to handle the closing (e.g., Md. Code Ann. Com. Law § 12-120(c); Minn. Stat. Ann. §507.45, Subd. 4; and Va. Code § 6.1-330.70 (lender may not require the use of a particular attorney, surveyor, or insurer)).

[14] It should also be noted that some states require that lenders provide borrowers at the time of closing with a detailed statement of each charge for a settlement service that the borrower is obligated to pay. See, e.g., Kan. Stat. Ann. § 17-5514; Mich. Comp. Laws. Ann. § 438.31b.

these state law provisions would still be applicable to such payments. Moreover, the state law prohibitions on lenders requiring the use of a particular insurer would likewise inhibit a lender from requiring the borrower to use the insurer it had selected for inclusion in its guaranteed package. None of these provisions may be preempted by the Secretary pursuant to § 18 of RESPA, 12 U.S.C. § 2616.

Section 18 provides that RESPA does not annul, alter or affect any person from complying with state laws on settlement practices "except to the extent that those laws are inconsistent with any provisions of this chapter, and then only to the extent of the inconsistency." (Emphasis added.) While the Secretary may determine when such inconsistencies exist, the Secretary may not determine that "any State law is inconsistent with any provision of this chapter" if the State law gives greater protection to the consumer.

Accordingly, the Secretary's ability to make preemption determinations under § 18 only comes into play if a provision of state law is inconsistent with a provision of RESPA as enacted by Congress. The state laws discussed above are not inconsistent with RESPA § 8 as enacted by Congress, or with any other provision of RESPA. Thus, the Secretary has no authority under § 18 to preempt state anti-kickback or anti-rebate laws, or state laws ensuring that borrowers may select insurance providers, in order to facilitate a lender guarantee/packaging regime that is a creature of HUD's regulations.

II. HUD SHOULD OBTAIN APPROPRIATE AMENDMENTS TO RESPA BEFORE LAUNCHING A LENDER GUARANTEE/PACKAGING REGIME.

While the previous sections have discussed HUD's exemption and preemption authority to encourage a lender guarantee/packaging regime, there is a broader concern regarding HUD's regulatory authority that deserves consideration. On a mater that has such enormous potential to create serious, adverse and, perhaps, unintended consequences for the continued healthy operation of the residential real estate market in the United States, HUD should be extremely cautious about setting sail on a regulatory endeavor that lacks both (i) clear legislative support, and (ii) the statutory infrastructure to support the new regulatory regime.

As HUD has come to appreciate, RESPA's rules are not only important to consumers, but affect in fundamental ways the operations of literally hundreds of thousands of business and firms located in every county in the United States. These enterprises deal with the most significant investments that most consumers ever make and seek to ensure stability, safety and efficiency in the buying, selling, and lending on the security of, real estate. As a consequence, changes imposed on these industries that are not the natural development of economic or technological forces can frequently threaten serious disruptions that may adversely affect both the industries and the customers they serve.

Moving the country to a regime of lender guarantees of packaged closing costs is a most significant governmental step with serious potential for disruption and dislocation. If HUD believes it is a desirable direction in which to move, it should ask the Congress for specific policy direction and for such amendments to § 8 and to other provisions of RESPA as may be appropriate and needed. These are major policy judgments for which appropriate statutory guidance and enforcement mechanisms are essential.

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NAHB
NATIONAL ASSOCIATION
OF HOME BUILDERS

ACROSS THE COUNTRY · HOME BUILDERS CARE

Testimony Of
F. Gary Garczynski,
Immediate Past President
On behalf of the
National Association of Home Builders
Before the
United States House of Representatives
Housing and Community Opportunity
Subcommittee of
Financial Services Committee
On
HUD's Proposal to Reform RESPA

February 25, 2003

Good afternoon Mr. Chairman, my name is Gary Garczynski. I am a homebuilder and developer from Woodbridge, Virginia, and much of my business focuses on redevelopment of urban areas and the inner ring of older suburbs. I am the Immediate Past President of the National Association of Home Builders. I am pleased to have this opportunity to testify today on behalf of the 205,000 member firms that comprise the NAHB federation.

Last summer, HUD published a proposal, which, if implemented, would significantly change its regulations pertaining to the Real Estate Settlement Procedures Act (RESPA). NAHB's comments focus on two major elements of HUD's proposal: changes in the nature and content of current requirements for disclosure of the costs of mortgage transactions to consumers -- the Good Faith Estimate; and, the addition of an option for lenders to offer a package of settlement services at a guaranteed cost – the Guaranteed Mortgage Package.

It is clear that HUD intends to increase the transparency and reduce the complexity of mortgage transactions by improving the disclosure of mortgage fees and expenses to consumers. NAHB applauds this initiative and believes the effort has great potential to simplify mortgage shopping and loan closings. The proposed changes should also lower mortgage transaction costs and help minimize unexpected charges at the time of loan settlement.

NAHB is working as an enthusiastic partner in efforts to expand homeownership opportunities, particularly for minority households. We view the RESPA changes proposed by HUD as important to advancing these efforts. The complexity and cost of the home financing process have been major impediments to increasing minority homeownership rates and HUD's proposed regulatory changes would do much to increase access to mortgage financing.

Any proposal as sweeping as the one HUD has undertaken is bound to raise some questions, and NAHB does have a few concerns with respect to some aspects of the Proposed Rule. NAHB's concerns relate mainly to the circumstances involved in processing mortgages for newly built homes, which typically involve a fairly lengthy loan origination process.

Good Faith Estimate

Under the requirements for the Good Faith Estimate, the Proposed Rule does not make clear when changes in the transaction warrant a new disclosure. Re-disclosure will be burdensome to lenders in a new construction environment, where the loan origination period, which covers the span from start to completion of the home, may last four to nine months or more. Many changes can, and normally do, take place during the construction process. For example: changes in the purchase price due to changes in the buyer's preferences on options; changes in the relative attractiveness of mortgage products; and, variations in the financial circumstances of the home buyer. Changes in the purchase price of a home directly impact the cost of document stamps and transfer taxes. Similarly, changes in the loan amount affect the fee charged for lender's title insurance. Changes in a home's sale price can also prompt home buyers to seek different loan products because of changes in the funds needed to complete the sale.

Guaranteed Mortgage Package

The concept of a Guaranteed Mortgage Package is appealing and could reduce consumer costs, primarily through originators' negotiations with settlement service providers. However, a guaranteed package that is determined at loan commitment and lasts until settlement on a new home transaction puts the packager in a position of excessive risk. This may lead the original packager to offer less competitive terms than packagers who have an opportunity to offer a package closer to the date of the projected loan closing. Wider tolerances in guarantees would be needed for a new home transaction where the price and loan amount often change dramatically over the construction period.

NAHB Recommendations for Financing Quotes on Newly Constructed Homes

For both the Good Faith Estimate and the Guaranteed Mortgage Package, NAHB proposes an alternative based upon a days-until-closing threshold for providing final quotes and guarantees. For example, a lender would provide preliminary estimates at initial application and then issue final, guaranteed estimates thirty or sixty days prior to closing. This procedure would be comparable to the timing of guarantees that would be made in financing an existing home purchase. Further, this solution would allow the customer sufficient time to shop again if the final package was deemed to be less competitive, while providing the lender an opportunity to adjust those components of the package that actually changed during the often significant duration since the original application.

Other Issues of Concern

There are a number of other issues that must be clarified or resolved prior to the implementation of the proposed RESPA regulations. Two areas of concern to NAHB are the Truth in Lending Act and state laws governing real estate transactions.

<u>Truth in Lending Act Issues</u>

Meaningful reform of the settlement process must address the requirements of the Truth in Lending Act. The Guaranteed Mortgage Package approach of reducing the loan offer to two numbers -- settlement package price and interest rate -- effectively eliminates the need for an APR calculation. To continue to calculate and disclose an APR would likely be confusing to consumers and may actually diminish the desired results under the Guaranteed Mortgage Package proposal. We are concerned that pricing agreements negotiated between service providers and packagers could subject the APR calculation to manipulation through a shifting of the cost of fees included in the APR to fees outside the calculation. Therefore, we recommend that Congress allow the Guaranteed Mortgage

Package to satisfy or replace Truth in Lending Act requirements for those mortgage transactions involving such a guarantee.

Conflict with State Laws

NAHB believes that the proposal may conflict with the laws in many states, particularly with regard to state anti-rebate statutes, which might prevent packagers from negotiating a better price for required items such as title insurance. In addition, many states have anti-affiliate laws that would prohibit firms that are affiliated with the lender from having products or services included in a Guaranteed Mortgage Package.

Conclusion

In closing, NAHB recognizes the effort HUD has put into correcting some salient shortcomings in an otherwise effective housing finance system. We strongly support the intent of HUD's efforts. However, loans for new homes, which represent more than a quarter of annual purchase mortgage originations, have unique characteristics that must be specifically addressed in any RESPA reform.

We are confident that, in drafting a final regulation, HUD will fairly address the concerns that have been expressed regarding the proposal. NAHB believes it is possible for HUD to increase the transparency of mortgage transactions by improving the disclosure of mortgage fees and expenses to consumers without disrupting mortgage services.

STATEMENT

OF

CHARLES J. MENDOZA

MEMBER, AARP BOARD OF DIRECTORS

FOR THE HEARING ON:

"SIMPLIFYING THE HOME BUYING PROCESS: HUD's PROPOSAL TO REFORM RESPA"

BEFORE THE

SUBCOMMITTEE ON HOUSING AND COMMUNITY OPPORTUNITY
OF THE
COMMITTEE ON FINANCIAL SERVICES

U.S. HOUSE OF REPRESENTATIVES

FEBRUARY 25, 2003
2128 RAYBURN HOUSE OFFICE BUILDING
WASHINGTON, D.C.

National Headquarters | 601 E Street, NW | Washington, DC 20049 | 202-434-2277 | 800-424-3410 | 877-434-7598 toll-free TTY

Good afternoon Chairman Ney, Ranking Member Waters, and Members of the Subcommittee on Housing and Community Opportunity. My name is Charles Mendoza. I am a member of AARP's Board of Directors.

I appreciate this opportunity to offer AARP's assessment of the U.S. Department of Housing and Urban Development's proposal to reform the Real Estate Settlement Procedures Act. We believe there is a clear need to simplify and improve the process of shopping for and obtaining home mortgages. AARP strongly supports the thrust of HUD's approach for reforming today's confusing settlement process.

For nearly a decade, AARP has been actively advocating for reform of RESPA with these objectives in mind. Many homebuyers are mid-life Americans buying a long awaited first home, or those who are trading up, and older Americans who are restructuring their households as they approach their retirement years. Unfortunately, the existing RESPA disclosure requirements have turned a virtue into a vice by inhibiting rather than facilitating competition for loan products and comparative shopping by homebuyers.

Chairman Ney, because of the importance and complexity of the issues being raised, I have attached to my statement a copy of AARP's detailed agency comments regarding the proposed RESPA reform rule. If space permits, I would like to request that our comment letter be made part of today's hearing record.

HUD's proposal contains three major provisions:

- enhanced disclosures of mortgage broker or loan originator compensation,
- revisions to the Good Faith Estimate system - often referred to as GFE Disclosure, and
- the availability of guaranteed mortgage packages that include guaranteed settlement costs and interest rates. This loan package is often referred to as the GMP option.

In the limited time I have to address the Subcommittee, I would like to highlight several key features of our agency comment letter as they relate to these provisions:

- First, AARP supports HUD's proposal to streamline and improve the Good Faith Estimate system and to create a new disclosure form to permit the offering of a Guaranteed Mortgage Package. The GMP package carries with it guaranteed loan terms and settlement costs;

- Second, we support HUD's proposal to streamline and improve the accuracy of the GFE option. The proposed changes will offer significant advantages to borrowers over the current system by creating greater certainty. The revised GFE will be especially beneficial for subprime borrowers who will receive firmer costs information without risk of losing important consumer protection rights;

- Third, we favor the GMP as a novel concept to promote true comparison shopping by providing certainty for consumers at an early shopping stage;

- Fourth, we strongly recommend, however, limiting the GMP package to the competitive "prime" market until knowledge regarding subprime market behavior becomes more standardized and reliable. Our concern is that the subprime market has not yet developed the required market information that is necessary for creating competitive pricing standards;

- Fifth, in our comments to the Department, we detail the need for clearer enforcement mechanisms for the GFE and the GMP; and lastly,

- We suggest revising the proposed GFE and GMP disclosure forms to improve their clarity and comprehensibility.

Arcane as the language of RESPA may be, the substance of RESPA is tied directly to a central component of the American Dream – the expectation that most Americans will be able to afford to own a home.

We appreciate the purpose served by this hearing in focusing public attention on an important rule-making proposal and process. I will close by saying that while a number of important and useful modifications can and should be made to the proposed RESPA rule before final promulgation by HUD, we strongly support the Department's efforts to move this rule forward.

I would be happy to answer any questions you may have.

AARP

October 28, 2002

Rules Docket Clerk
Office of the General Counsel
Room 10276
U.S. Department of Housing and
Urban Development
451 Seventh Street, S.W.
Washington, D.C. 20410-0500

Re: Comments on the proposed RESPA rule to simplify and improve the process of obtaining mortgages to reduce settlement costs to consumers per 67 Fed. Reg. 49134 (July 29, 2002).

[Docket No. FR-4727-P-01]

Dear Sir or Madam:

AARP appreciates the opportunity to offer its comments to HUD on its Proposed Real Estate Settlement Procedures Act (RESPA) Rule to simplify and improve the process of obtaining mortgages to reduce settlement costs to consumers. 67 Fed. Reg. 49134 (July 29, 2002). AARP has worked with HUD on this issue for many years and is gratified that HUD has taken a giant and creative step forward to protect consumers in their mortgage transactions. AARP congratulates HUD on its insightful approach to reforming the GFE and its bold foray into guaranteeing costs and interest rates for consumers of home mortgages.

HUD's proposal is extensive and comprehensive. AARP's comments, are of necessity, lengthy as well. AARP supports HUD's decision to modernize the home mortgage market and streamline disclosures and offers its constructive comments to advance HUD's laudable goals. AARP offers constructive comments to bolster and solidify this innovative and exciting proposal.

AARP's comments are presented in three sections:

- GFE–Good Faith Estimate;
- GMP–Guaranteed Mortgage Package;
- Other miscellaneous comments.

In these sections, AARP offers an analysis of the relevant form, proposes its own simplified and revised form (as presented in Appendices I and II), offers additional comments and responds to the relevant questions posed by HUD.

As HUD has very publicly recognized, its novel proposal does not address or seek to remedy the very real problems presented by predatory mortgage lending. AARP pledges to continue to work with HUD to combat these problems and eliminate the scourge of predatory lending. To further this goal AARP proposes that the GMP be tested first in the competitive prime market. At the same time, AARP will work with HUD to create conditions that will further competition in the subprime market and improve the financial literacy of homeowners in that market. AARP is very mindful of the abuses of predatory lending and their disproportionate impact on older Americans. AARP's comments seek to ensure that the proposed Rule does not inadvertently exacerbate this problem.

GOOD FAITH ESTIMATE

AARP applauds HUD's efforts to undertake reform of the GFE disclosure. The complexity of the mortgage marketplace makes estimating and disclosing potential costs a great challenge. Indeed, one of the original driving forces behind mortgage reform was the need to merge or consolidate the disclosures required by RESPA (the GFE and HUD-1) and by the Truth in Lending Act (TILA). This was thought to be beneficial both to the mortgage industry and to consumers because it would streamline the federal disclosures and at the same time make them more transparent. In addition, AARP and others pointed out that the oblique disclosure of payments from the mortgage lender to the broker put a veil over the underlying nature of the transaction and deprived the borrower of the ability to choose the structure of his/her own mortgage.

Our comments on the GFE are presented in three parts. Part I offers comments that correspond to the sections in the proposed GFE form. Part II presents AARP's responses to HUD's questions regarding the GFE. A proposed revised GFE is attached as Appendix I.

GFE: Part I The GFE Form

It is clear that the GFE needs to be updated. We believe the proposed GFE form could be further simplified to make it a more user-friendly tool consumers need. AARP suggests that consumer understanding of the critical information offered by the GFE would be greatly enhanced by the following changes:

I. OUR SERVICES. AARP recommends that this section be eliminated for several reasons:

- The cost information in the form speaks for itself; the additional verbiage does not add clarity to the transaction. In fact, the information under III.A., which states how much the originator is charging the consumer, will do more to clarify the originator's arm's length role than any descriptive paragraph could.
- The language in this section of the form is too legalistic and uses terminology unfamiliar to consumers. For example, the terms, "loan originator" and "funding source" are not part of common vocabulary.
- Any general description of the originator's role may be inaccurate as, for example, some originators may be acting as agent, etc.; as a result, this section does not

advance the consumer's understanding of the originator's role.

On the other hand, the language, "You should compare the prices in the boxes below and shop for the loan originator,[1] mortgage product, and settlement services that best meet your financing needs" should be retained either in this location or elsewhere on the GFE. The proposed underlined language sends the message that consumers need to shop in order to obtain the best prices; it is so important that HUD may wish to focus the consumer's attention on it by using bold lettering or some other device or even by placing it as a legend on each page of the GFE.

II. LOAN TERMS. This section should be retitled to read, "ESTIMATED LOAN TERMS": AARP believes that it is important to highlight the differences between the GFE and the GMP. It is therefore essential to make clear to the borrower that, unlike the GMP, all aspects of the loan described in the GFE are estimates and the loan terms are not guaranteed. At the same time, the estimated loan terms do form the basis for the transaction between borrower and lender/broker and it is therefore useful to require that they be disclosed on the front page of the GFE in an easy to read format. We suggest the following layout with the addition of boxes that can be checked to indicate whether those elements are included in the proposed loan terms:

[1] As discussed, the term, "loan originator" is not part of everyday language and should be replaced with "lender or mortgage broker."

Mortgage Amount: ___________
Interest Rate: ___________

- ☐ Fixed
- ☐ Adjustable

Term of Loan:___________ (years)
Number and dollar amount of monthly payments___________
including:

- ☐ principal
- ☐ interest
- ☐ mortgage insurance
- ☐ real estate taxes
- ☐ hazard insurance

If an adjustable rate loan, maximum monthly payment $ _________

- ☐ Balloon payment: $ __________ due on ____
- ☐ Maximum prepayment penalty $__________

It is important to display all loan terms in the same location to avoid consumer confusion and the opportunity for bait and switch. Displaying all important loan terms on page 1 will facilitate accurate comparison shopping. For example, the proposal to display some loan terms on page 2 is likely to have the unintended consequence of leading some consumers to conclude that a proposed 15 year balloon mortgage loan is really a 15 year amortizing mortgage loan because the balloon is not shown on page 1. In addition, a consumer may unwittingly compare two different 15 year loans and conclude that one with a slightly higher interest rate (but no balloon) is a better loan, because of the failure to identify the balloon on page 1. To the extent that unscrupulous lenders or brokers wish to deceive borrowers about certain terms of their loans, separating the loan terms, particularly those that are associated with predatory loans (such as balloons, prepayment penalties and adjustable rates) facilitates that deception.

We believe that certain other disclosures should be added, while others may be able to be deleted. For a loan with a prepayment penalty, it is important for the consumer to know what is their maximum exposure. It may well be that a consumer would be willing to trade off a lower interest rate for a relatively inexpensive prepayment penalty. However, few consumers would knowingly agree to a loan with a prepayment penalty that could cost as much as 6 monthly payments–a common feature of predatory loans. In order to enable consumers to make that comparison we recommend that the maximum prepayment penalty be shown as a dollar amount.

Adjustable rate loans should similarly be disclosed on page 1. We recommend that these disclosures be reduced to only the most critical elements: initial rate, initial monthly payment and maximum monthly payment. It is the maximum monthly payment that is of greatest interest to the consumer and the number that will best enable comparisons between other adjustable rate loans and fixed rate loans. In our experience in litigating predatory lending cases, consumers are often unaware that they have a loan whose rate can adjust, but even when they are "aware" they have been persuaded that the payment cannot increase very much. Providing the maximum monthly payment will enable consumers to see their maximum exposure and assess whether that is a risk they are willing to take. Similarly, we would delete the additional disclosure of the percentage that is attributable to mortgage insurance and simply indicate (by checking the applicable box) that mortgage insurance is included in the monthly payment.

III. <u>SETTLEMENT COSTS</u>. HUD's proposed reduction of disclosed settlement costs to eight categories is a significant improvement over the current GFE. AARP believes that several additional categories of costs can be combined, further simplifying the GFE and contributing to enhanced consumer comprehension. AARP recommends reducing the number of categories of settlement costs from the proposed eight to the following three categories:

- **Net Charges By Broker and Lender**
- **Title and Settlement Services**
- **Other Necessary Charges.**

Net Charges by Broker and Lender. AARP recommends changing, "Origination Charges" to "**Net Charges by Broker and Lender:**"

- "origination charges" is a creature of regulation, but will not be understood by average consumers.
- it is important to use plain language to increase consumer comprehension.
- calling this category what it is–charges by the broker and lender--would be more easily understood by consumers.

Title and Settlement Services. AARP recommends merging categories C, D, & E into one category of title and settlement services. The only distinction among lines C, D & E is whether the lender will require the use of a particular third party or in-house provider for a particular service or whether it will allow the consumer to shop for that service. As currently structured, the separation into three categories can lead to problems:

- lack of comparability--since each lender will be free to determine what services are required versus shoppable, dividing these services into three cost categories will undermine comparability and inhibit comparison shopping;
- confusion among borrowers--GFEs from different lenders can include the same services in different categories–for example, one lender may require the use of an identified appraiser and therefore include the appraisal cost in category C, (and identify it as required on the attachment) while another GFE may permit shopping among a group of appraisers and therefore include the cost in category E (and identify it as "shoppable" on the attachment).

While AARP recognizes the desirability of holding loan originators to their estimates whenever possible, we believe that comparison shopping would be facilitated and confusion among borrowers reduced by combining all charges into one line entitled "**Title and Settlement Services.**" Even if HUD should decide to permit a tolerance of up to 10% on the entire category. any resulting ambiguity should be outweighed by the benefits of transparency and comparability. A breakout of services and an identification of services that can be shopped for can continue to be provided on Attachment A-1.

Other Necessary Charges. A third category should be created inclusive of F, G, H, & I and borrower's title insurance. A 10% tolerance would apply to these charges as well.

In addition to reducing the number of categories on the GFE, AARP would eliminate the references to the lines of the HUD-1 that are proposed to be located next to each category of settlement costs on the GFE. At the GFE stage, the consumer has no frame of reference for the line numbers referred to on the HUD-1. As such, these references add a level of intricacy to this already complicated disclosure without contributing to the consumer's understanding. This suggestion is not intended to affect any instructions regarding the proper allocation of fees on the HUD-1. It simply suggests that the consumer will find that information more confusing than beneficial at the GFE (shopping) stage.

III. A. **Origination Charges** and III. B. **Interest Rate Dependent Payment.** We commend HUD for including these sections on the GFE to better inform the consumer about the true amount of charges that are being imposed to originate his/her mortgage loan. We hope that the transparency provided by these disclosures will create downward pressure on mortgage costs. Including this breakdown of information is an extremely important step toward assuring that consumers receive the benefits that should accrue to them from increased interest rates. It should promote more shopping and consumer scrutiny of lender and broker charges. This information educates consumers on the relationship between interest rate and origination costs and sets the stage for allowing consumers to select among three loan choices displayed on page 2.

AARP applauds HUD's identification of the yield spread premium as money that belongs to the borrower. This designation reflects the reality that the yield spread is a cost to the consumer of making the loan and only the consumer can direct how it is to be used. AARP believes that there has been extensive abuse of the yield spread premium by brokers and lenders up to this point in time resulting in unnecessarily high costs to consumers. While we do not believe that this will protect the most vulnerable borrowers, whose interest rates are often increased dramatically without any corresponding benefit, we believe it will enhance the ability of many consumers to use the yield spread premium to reduce or eliminate out of pocket costs on their loans.

We would combine sections III.A and III.B., "**Net Broker and Lender Charges.**" In addition, AARP recommends that the sub-categories be descriptive phrases, in plain English to facilitate consumer comprehension. We think this clarification will enhance the borrower's understanding of how his/her choice of loan terms affects the yield spread premium or discount points charged on the loan.

Proposed language:

III. SETTLEMENT COSTS:

A.	**Net Charges by Broker and Lender**		**$500**
	1. Lender and Broker **Charges** (owed by borrower) *(See Attachment A-1)*	$2,000	
	2. Payments Based on Your Interest Rate		
	(a) Additional amount borrower will pay toward **Charges** (reduces interest rate) +	$ 0	
	(b) Amount lender will pay toward **Charges** (Because of increased interest rate) -	$1,500	
		$ 500	
B.	**Title and Settlement Services** *(See Attachment A-1)*		**$1,500**
C.	**Other Necessary Charges**		**$500**
Net Settlement Costs Due From Borrower (cash to close)			**$2,500**

IV. OPTIONS TO PAY SETTLEMENT COSTS AND LOWER YOUR INTEREST RATE

AARP applauds HUD for including this section which both educates consumers about the relationship among interest rate, financed payments and cash payments at closing and offers them choice in selecting terms best suited to their needs. As AARP has maintained for many years, offering the consumer a range of choices is critical to informed decision making. We are therefore encouraged that HUD has chosen to provide consumers with three alternative loan choices. AARP is hopeful that offering consumers these choices is a first step that will improve consumers' ability to shop in the subprime market.

We are suggesting an alternative format for presenting the three loan choices. We believe that consumers will find it easier to understand and use this information if it is presented in an easy-to-read format, such as we have suggested for II. Estimated Loan Terms and III. Settlement Costs rather than in a grid format. In addition, we agree with HUD that the three loan offers should be tailored to the individual consumer and should not be generic examples. We believe that all originators should be required to present these three choices in a uniform manner so that consumers can comparison shop. We are including five choices to show a greater range of loans that an originator might offer to a consumer. Among these choices we have also included one loan in which a consumer would obtain a lower interest rate (and no yield spread premium) in exchange for agreeing to a prepayment penalty. AARP is concerned that consumers not be compelled to accept a prepayment penalty. We believe that HUD should require originators to offer at least one loan choice without a prepayment penalty.

AARP would substitute the format below for the grid in IV. We would retain the descriptive language that precedes the grid.

Your loan will cost $2,000 in Charges by Broker and Lender and an additional $2,000 in Settlement costs for a total of $4,000. You have several choices about how to pay for these costs.

Choice #1-- Lender will pay $1,500 toward the Charges by Broker and Lender
You will pay a total of $2,500 at closing:
$500 for Charges by Broker and Lender,
+ $2,000 for settlement costs at closing.

Loan terms of:
(same as choice on page 1)
Mortgage Amount: $100,000
Interest Rate: 7 %
- ▪ Fixed
- ▫ Adjustable

Term of Loan: 30 (years)
Number and dollar amount of monthly payments: 360 payments of $ 665.30
If an adjustable rate loan, maximum monthly payment $ __________
- ▫ Balloon payment: $ 0
- ▫ Maximum prepayment penalty $ 0

Choice #2 – Lender will pay $2,500 toward the Charges by Broker and Lender
You will pay a total of $1,500 at closing:
-$500 for Charges by Broker and Lender,
+ $1,500 for settlement costs at closing.

Loan terms of:
Mortgage Amount: $100,000
Interest Rate: 7.25 %
- ▪ Fixed
- ▫ Adjustable

Term of Loan: 30 (years)
Number and dollar amount of monthly payments: 360 payments of $ 682.18
If an adjustable rate loan, maximum monthly payment $ __________
- ▫ Balloon payment:__________
- ▫ Maximum prepayment penalty $ 0

Choice #3 -- Lender will pay $ 0 toward the Charges by Broker and Lender
You will pay a total of $4,000 at closing:
$ 2,000 for Charges by Broker and Lender,
+ $2,000 for settlement costs at closing.

Loan terms of:

Mortgage Amount: $ 100,000
Interest Rate: 6.75 %
- ▪ Fixed

- ☐ Adjustable

Term of Loan: 30 (years)
Number and dollar amount of monthly payments: 360 payments of $ 674.54
If an adjustable rate loan, maximum monthly payment $ __________

- ☐ Balloon payment:___________
- ☐ Maximum prepayment penalty $ 0

Choice #4 -- Lender will pay $ 0 toward the Charges by Broker and Lender
You will pay a total of $4,000 by borrowing an additional $4,000 in your loan
$2,000 for Charges by Broker and Lender,
+ $2,000 for settlement costs at closing.
Loan terms of:

Mortgage Amount: $ 104,000
Interest Rate: 6.75 %

- ▪ Fixed
- ☐ Adjustable

Term of Loan: 30 (years)
Number and dollar amount of monthly payments: 360 payments of $ 674.54
If an adjustable rate loan, maximum monthly payment $ __________

- ☐ Balloon payment:___________
- ☐ Maximum prepayment penalty $ 0

Choice #5 -- Lender will pay $ 0 toward the Charges by Broker and Lender
You will pay a total of $4,000 at closing:
$2,000 for Charges by Broker and Lender,
+ $2,000 for settlement costs at closing.
Loan terms of:

Mortgage Amount: $ 100,000
Interest Rate: 6.25 %

- ▪ Fixed
- ☐ Adjustable

Term of Loan: 30 (years)
Number and dollar amount of monthly payments: 360 payments of $ 615.72
If an adjustable rate loan, maximum monthly payment $ __________

- ☐ Balloon payment:___________
- ☐ Maximum prepayment penalty $ 1,500.

V. ADDITIONAL LOAN TERMS. AARP believes that all important loan terms should be disclosed in a consolidated form on page 1. We would delete this section.

GFE: Part II AARP'S Responses to HUD Questions 1-11
(HUD's questions are in *italics*; AARP's responses are in **bold**)

1. *As proposed in Section III. A. (1), the proposed GFE form would briefly explain the originator's functions and that the borrower, not the originator, is responsible for shopping for his or her best loan. Does the language proposed adequately convey this message? If the commenter thinks otherwise, it should provide alternative language for the form that better explains the loan originator's function to the borrower. Should the form also address agency requirements under state laws and how?*

   The proposed language is confusing and does not assist the borrower in understanding the transaction or the "originator's" role. In addition, to the extent that state law decrees otherwise or to the extent that the borrower and the originator agree to a fiduciary relationship, the language is inaccurate. We think this form should be as simple and clear as possible. As a result, we would delete this section in its entirety and retain only the underlined language that encourages shopping. See comments above.

2. *In Section III.B.(2) c., the proposed rule requires that the amounts estimated on the GFE for mortgage broker and lender origination charges may not vary at settlement absent unforeseeable circumstances. Should the rule provide for this "unforeseeable circumstances" exception? Are the particular circumstances specified in HUD's formulation in this proposal sufficiently encompassing? What evidence should a broker or lender be required to retain to prove the existence of such circumstances and justify any increase in charges at settlement?*

   AARP believes that this exception is unnecessary and is concerned that it may encourage lenders/brokers to game the system. For example, it is difficult to understand why a flood would cause broker compensation to change or how it could affect government recording fees which are fixed. In addition, there is no indication as to what level of proof would be required that a particular disaster necessitated the increased charge. Is it contemplated that a disaster must be local in order to permit an increased charge or would lenders/brokers throughout the country have been able to use events of 9/11 to increase charges, whether or not their local economy was affected? While we believe the proposed exemption is unnecessary and could promote litigation, if HUD chooses to allow it, it should create a rule that sets clear standards and imposes strict document retention requirements.

3. *In Section III.B.(2)c., the proposed rule establishes a 10% limit, or "tolerance," for categories of settlement services and costs including third party services that the borrower shops for and escrow/reserves by which such costs cannot exceed the GFE estimates by 10% at settlement absent unforeseeable and extraordinary circumstances. It also establishes zero tolerances for origination charges and lender required lender selected third party costs and government charges that cannot vary from the estimate through settlement absent unforeseen circumstances. Are these appropriate tolerances and tolerance levels or should other tolerances/tolerance levels be established for these*

categories? Also, should a tolerance be established for borrower's title insurance? What alternative or additional means might be employed to ensure that loan originators take the care necessary to complete the GFE to ensure that it represents a Good Faith Estimate of final settlement costs?

In AARP's experience, GFEs are often the subject of abuse and even a tool in the arsenal of the bait and switch predatory lenders. The problems range from providing multiple and conflicting GFEs, to understating the actual costs of the loan, to failing to provide the GFE until the date of settlement. AARP believes that most of the tolerances built into the proposed Rule will force brokers and lenders to take the representations of the GFE more seriously and will assist borrowers in comparison shopping, in both the prime and subprime markets.

AARP supports zero tolerances for origination charges. It is completely reasonable to require lenders and brokers to be aware of and fix their own charges from the outset. This is particularly important in the subprime market where the most egregious abuses occur. While we support HUD's decision to reduce to the greatest extent possible the wiggle room that currently exists for other settlement charges, AARP believes (as discussed above) that a tolerance of as much as 10% could be allowed for the entire category of AARP's proposed category, Title and Settlement Services, even if those services and providers are required by the lender. AARP does not support tolerances in excess of 10% for any provider selected or suggested by the originator, or for any other easily ascertainable charges. These would include owner's title insurance and per diem interest.

HUD's position that all fees be returned if final costs exceed tolerances would assist in ensuring accurate GFEs but would not assist borrowers who are unable to walk away on the settlement date. HUD could require a rebate of any fee that exceeds tolerances on GFE. In addition, AARP recommends that HUD identify as an "unfair and deceptive practice" the charging of any fee at settlement that exceeds the tolerance established in the Rule.

4. *In Section III. B.(2) d., the proposed rule would amend Regulation X to make clear that loan originators may enter into volume arrangements where such discounted prices are charged to their customers. Commenters are invited to provide their views on the ramifications, if any, of this clarification.*

AARP agrees that RESPA permits an originator to negotiate volume-based discounts, as long as they are passed on to the borrower.

5. *In Section III. B. (2) c., the proposed rule requires that the tolerances will apply to the GFE from the time the form is given by the loan originator through settlement. Also, in case it takes a substantial time for the borrower to decide to use the loan originator from the date the form is given, the rule and the form provide that the GFE need only be open for borrower acceptance for a minimum of 30 days from when the document is delivered or mailed to the borrower. After that time, the GFE could be ratified or superseded by the*

originator at the borrower's request. Is this expiration date appropriate to protect against unnecessary costs flowing from an indeterminate liability or for other reasons?

Yes.

Is 30 days too long or too short?

AARP believes that 30 days is a reasonable amount of time for a borrower to shop and to make a decision to select a loan product and originator.

Another possibility that commenters may consider is whether the numbers on the GFE should apply only from the time the borrower enters into an agreement with the loan originator.

We do not understand how this idea would assist borrowers in shopping. If the GFE numbers do not apply during the shopping period, they serve no purpose in promoting shopping. Instead, this would provide an opportunity for bait and switch since new numbers could be presented at the time the borrower enters into an agreement with the originator and commits to paying money. HUD's effort to promote shopping, which is particularly important in the subprime market, would be undermined by making this change in the proposed rule.

HUD also invites commenters' views on whether HUD now should require a borrower's signature on the GFE to memorialize acceptance and begin the period during which the estimates are binding.

AARP believes that it would be inappropriate to require the borrower's signature as a prerequisite to making the GFE estimates binding. Again, that procedure suggests that a borrower would not have reliable estimates with which to shop among different originators. Similarly, it is unclear what effect is contemplated by requiring the borrower's signature or what is meant by the phrase, "to memorialize acceptance." Surely a borrower could not be held to a commitment to enter into a loan with a particular originator without a firm commitment from the loan originator as to interest rates, loan terms, etc. Moreover, under current practice, borrowers remain free to shop among originators and lose their application fees if they find a more favorable loan. HUD's expressed intent in revising the GFE to encourage shopping and competitive pressure on pricing could be undermined by a signature requirement. Similarly, AARP is concerned that some originators might use the signature requirement to game the system, for example, by intentionally neglecting to obtain borrower signatures. Such originators, under this alternative proposal, would retain the ability to reset fees and undermine the intent to hold originators more strictly to their estimates on the GFE.

6. *In Section III. B. (1)b., the proposed rule simplifies the GFE by placing all loan origination costs in a small number of primary categories. This is intended to facilitate borrower understanding and shopping of major loan costs and minimize*

the proliferation of "junk fees" and duplicative charges. How could the GFE be made even simpler to facilitate borrower shopping?

AARP applauds HUD for simplifying the GFE. As discussed in our comments above, AARP has proposed several ideas for further streamlining the GFE.

7. *In Section III. A. (3), the proposed rule requires that on the front of the proposed form mortgage brokers disclose the lender credit right below the total origination charges to: (a) make the borrower aware of the effect that the credit has to reduce total origination costs; (b) avoid confusion among borrowers; and (c) avoid giving any competitive disadvantage to either a broker or lender for the same loan. What, if any, other approach to address these concerns is better and why?*

See AARP's comments above which suggest a different and more easily understandable method of disclosing the yield spread to the borrower.

Should the new GFE form disclose this credit at the bottom of the proposed form because the credit can be applied to all settlement costs?

AARP believes that it is preferable to retain the credit in the proposed location. That makes it clear that the yield spread is a method of paying the loan origination fees. The yield spread might also be used to offset some or all of the settlement costs. This could occur in a brokered transaction if the yield spread exceeds the total origination fees; such a credit would be shown as a negative number, which would offset some or all of the settlement costs listed below.

8. *As proposed in Section III.A.(3), as another step to avoid borrower confusion and any competitive disadvantage among lenders and brokers, the proposed rule breaks out on Attachment A-1, rather than on the front of the proposed form, the "Loan Origination Charges" into "Lender Charge" and "Broker Charge." How, if at all, does this approach advantage or disadvantage either lenders or brokers or confuse borrowers in comparison shopping? Would the industry and borrowers be better served if there is a breakout of "Lender charges" and "Broker charges" on the front of the form and why?*

No, it is important to keep the form as simple as possible. It really shouldn't matter who among the originators is receiving the charges, as long as borrower can see the total cost and compare it to costs of other originators.

9. *As proposed in Section III.B.(2) e, the new GFE will consolidate certain charges into lump sum categories (e.g. lender required third party services). To permit the borrower to compare the new GFE to the HUD-1, it will be necessary for HUD to establish additional instructions to guide the reader so that the new GFE could be compared to the HUD-1. Would it be better to change the HUD-1 so the fee categories correspond to the groupings on the GFE and the two documents can be*

more easily compared?

Possibly, but only after simplifying the GFE (as suggested above) so that it is more readable and understandable.

If commenters support changes to the HUD-1 to make it more comparable to and compatible with the new GFE, how extensive should these changes be and in what areas? Should the HUD-1 continue to list all charges for services or should it also be shortened and simplified as well to cover only categories of services?

It could present a problem for TILA compliance/remedies if certain charges were lumped together.

10. *Should a safe harbor from Section 8 scrutiny be established for transactions where the mortgage broker signs and contractually commits to its charges on the GFE?*

No. AARP has never supported a Section 8 exemption for fixing a mortgage broker's fee. Throughout the years of discussion of this issue, the lynchpin of AARP's support for such an exemption as applied to a mortgage broker has always been that a broker must fix the fee and offer the consumer choice in paying it by presenting three choices of interest rate and costs to close.

The purpose of proposing this safe harbor would be to encourage a firm contractual commitment to borrowers, before they pay a fee and commit to a particular mortgage broker, so that the borrower can shop among mortgage brokers. Considering the proposed changes to the GFE, the proposed packaging safe harbor and HUD's current guidance on mortgage broker fees, is this safe harbor necessary for industry or borrowers and why?

AARP does not believe that fixing a broker fee confers a benefit on the borrower that would justify depriving the borrower of a Section 8 remedy. HUD's GMP proposal would enable mortgage brokers to avoid Section 8 liability while conferring a benefit of certainty as to interest rate, mortgage terms and settlement costs that would not be available to consumers who do business with mortgage brokers who fix only their own fee.

In light of the proposed rule's other provisions is any other additional disclosure for mortgage brokers warranted, such as an additional statement of what the broker's fees are and how they function? **No.**

<u>GUARANTEED MORTGAGE PACKAGE</u>

AARP applauds HUD's foresight and innovation in introducing a novel concept to promote true comparison shopping for consumers in the competitive marketplace. Introduction of the GMP as a method of offering mortgages will benefit both consumers and lenders by providing certainty to consumers at an early stage of shopping in exchange for offering lenders a clear path for compliance with Section 8 of RESPA. The GMP system will offer lenders an incentive to return to a simpler method of disclosure, while offering borrowers the certainty of fixing rates and closing costs and encouraging meaningful shopping.

For the vast majority of prime borrowers, the certainty offered by the GMP will exponentially enhance consumer understanding and thus promote real comparison shopping. This is a significant benefit to consumers who truly shop. At the same time, the GMP consumer will be deprived of the valuable remedy offered by RESPA, Section 8 (and likely certain remedies under TILA). It is, therefore, critically important to ensure that the interest rate, closing cost and mortgage term promises contained in the GMPA are real commitments that can be relied upon and enforced by the consumer. Because the trade-off of certainty for consumers means a corresponding loss of consumer protections under RESPA and likely under TILA, it is important to carefully examine the parameters of the GMP system. AARP believes that existing conditions in the subprime market warrant an initial restriction of the GMP to the more competitive prime market. However, AARP is committed to working with HUD, the mortgage industry and our fellow consumer advocates to develop the necessary market indicators that will allow subprime as well as prime borrowers to benefit from having the GMP choice.

AARP offers its comments to clarify the process and the premises which are essential to a workable GMP system. The Comments are presented in three parts. Part I presents comments that correspond to the sections in the proposed GMP form. Part II present general comments on the boundaries of the GMP, enforcement and reconciliation of TILA and RESPA. Part III provides responses to questions posed by HUD in connection with its GMP proposal.

<u>GMP: Part I The GMPA Form</u>

The GMP is based on the borrower's representations regarding income, assets, home value and any other information requested by the entity offering the GMP. It is important to make these premises clear on the face of the document. Similarly, the GMP is premised on the packaging entity's having performed a credit analysis. Because this information forms the basis for the offer in the GMPA, it should be spelled out in the form with a simple statement such as:

"The guarantees offered in this Guaranteed Mortgage Package Agreement are based on:

- you (the borrower(s)') statements that your gross monthly income is $ and that the value of the home you seek to [purchase] [refinance] located at ____________ is $____; and
- on a credit analysis performed by the Packager. This Agreement is subject to final verification of your credit rating, the value of the property and your income and other information provided by you."

Packaging entities would be free to attach any additional information provided by the borrower on which the entity based the offer contained in the GMPA. Stating the predicates to the offer and clarifying that the offer is made after credit analysis by the Packager will help discourage bait and switch tactics. This will also further clarify that the offer is subject only to verification of the information provided by the borrower.

I. <u>INTEREST RATE GUARANTEE</u> AARP wholeheartedly endorses the guaranteeing of interest rate, costs and mortgage terms to borrowers at the shopping stage. As discussed below, and as HUD has recognized, the guaranteeing of the cost of a package of settlement services, without a corresponding interest rate guarantee, is an empty promise, since it leaves the originator free to shift additional costs to the interest rate. AARP congratulates HUD for recognizing that these components are inextricably connected in a mortgage and structuring the GMP accordingly.

As with the GFE, AARP believes the GMPA form could be made more readable and more transparent to consumers. Consistent with our comments on the GFE, we believe the prominent disclosure of adjustable rate information and balloon payments in the same location as the other loan terms is critical and that a disclosure of the loan term in years, in addition to number of payments would assist borrowers in understanding the offer. AARP would also recommend including a disclosure that no prepayment penalty is included in the loan.

In AARP's experience, prepayment penalties are often a feature of predatory mortgage loans and are rarely included in prime loans. As a result, and as discussed in greater detail below, we recommend that the GMP not be available for loans that contain prepayment penalties. We nevertheless recommend that the *absence* of a prepayment penalty be included with other mortgage terms for two reasons:

- to make absolutely clear to the borrower that no prepayment penalty is included, and
- to permit borrowers to make a side by side comparison of GFE and GMP offers.

We suggest the following format for the Interest Rate Guarantee which is analogous to the format suggested for the Estimated Loan Terms in the GFE and which would enable consumers to make side by side comparisons of offers through the GFE and through the GMP.

<u>I. INTEREST RATE GUARANTEE</u>

We guarantee to provide you with a loan on the following terms:

Mortgage Amount: ___________
Interest Rate: ___________
- ❑ Fixed
- ❑ Adjustable

Annual Percentage Rate:________
Term of Loan:___________ (years)
Number and dollar amount of monthly payments____________
the monthly payment includes payments only for those items that are checked:
- ❑ principal
- ❑ interest
- ❑ mortgage insurance
- ❑ real estate taxes
- ❑ hazard insurance

If an adjustable rate loan, maximum monthly payment $ _________
❑ Balloon payment: $__________

No prepayment penalty

We have proposed several technical changes to the section in part I. of the GMPA that informs the consumer of the time limits for shopping and acceptance and explains how the guarantee functions during and after the shopping period. Once a consumer is provided a GMP, the guaranteed interest rate can float only in precise relation to an identified index during the shopping period (minimum 30 days). Similarly, the guaranteed rate is tied to an index in the period after acceptance and prior to lock-in. As we understand it, for any given consumer, a packager would be tied to the same index and margin for lock-in during the shopping period and lock-in at a later date, a minimum of 60 days. Any other method of float would defeat the interest rate guarantee and would be unacceptable. The changes we have proposed to the GMPA clarify this point by creating a single disclosure as to how the guaranteed interest rate floats.

AARP believes that any index used by a packager should be easily available in the consumer's market, preferably in a local newspaper, and that the GMPA should inform the consumer where to find the index and how to use it. We have also included alternate language that would allow a packager to tie its rate to a specific product on its matrix, so long as that matrix is published and readily accessible by the consumer (without a need to access a computer). Should HUD permit packagers to use this alternate method of guaranteeing the rate, the packager should also explain on the GMPA where the consumer can access that information and how to use it.

Proposed language:

☐ The interest rate is guaranteed through settlement if you accept and sign this agreement now and lock-in the rate by ___________[date/time].

☐ If you accept and sign this agreement by ______ [30 days or more], we guarantee that the interest rate will not exceed ___ over _____[index] rate at the time of lock-in. [60 days or lender's time limit on lock-in]. You can easily check your rate by locating the index __________[where] and doing the following calculation:______________.

☐ [Alternative language] The loan product we have offered you is our ____ product. If you accept and sign this agreement by _______ [30 days or more], we guarantee that you will receive the interest rate that we are offering to our customers for our ___ loan product [same product as that identified above] at the time you lock in [60 days or lender's time limit on lock-in]. You can easily check those rates by _______________.

If you do not accept by ______, this offer will expire.

II. <u>GUARANTEED MORTGAGE PACKAGE</u>, III. <u>OTHER REQUIRED SETTLEMENT COSTS</u> and IV. <u>OPTIONAL OWNER'S TITLE INSURANCE.</u>

As we commented in connection with the GFE, AARP believes that a more simplified format with less verbiage and a clearer presentation of the costs would be more useful to the consumer. We have simplified that format on a proposed revised form that is attached.

V. OPTIONS TO PAY SETTLEMENT COST & LOWER YOUR INTEREST RATE.

As AARP has commented in connection with the proposed GFE, this section offers a critical opportunity to educate the borrower regarding his/her options to buy down the interest rate by paying discount points, or to reduce out of pocket costs by financing them into the principal of the loan and/or by buying up the rate. We believe this part of the GMP to be essential to promoting borrower choice and to decreasing the opportunities for packagers to bait and switch the consumer. We again suggest that the three loan choices in this section be presented in the same format as we have suggested for the GFE and for the Interest Rate Guarantee on the GMPA. Requiring lenders/packagers to present mortgage loan information in a uniform format will significantly advance the Secretary's stated goals of encouraging consumers to comparison shop for their mortgage loans. We present this format in the attached revised form.

Because the GMP presents loan choices somewhat differently from the GFE, we have also suggested that the introductory material contained in A., B., C., and D. be customized for each consumer. For example, following HUD's proposed language in C., we would add information that discloses to the consumer the relationship between buying up the interest rate and the reduction in cash to close. We also suggest allowing the packager to describe the limitations, e.g. the maximum rate increase that it would accept.

"**C. Pay Settlement Costs Through a Higher Interest Rate: . . .** You can reduce the cash you need to bring to closing by $500.00 in exchange for every increase in your interest rate of 1/8%. You can reduce your cash payment by a maximum of $2000 which would add 1/2% to your interest rate."

Similarly for "**D. Lower Your Interest Rate. . .** You may decrease the interest rate 1/8% for every $500 additional cash you bring to settlement. You can decrease your rate by a maximum of 1/2% for a payment of $2,000."

This information will assist borrowers in understanding the origin of the choices presented and how the GMP and interest rate guarantees interact.

The following example is taken from one of the choices presented on our revised GMPA:

Choice #2: GMP: $1500 + other required services: $2000 = $3,500 minus $1000 to increase the interest rate by 1/4% [from 6.75 to 7] = **$2,500 cash to close**

Loan terms of:
Mortgage Amount: $100,000
Interest Rate: 7 %
- ▪ Fixed
- ❑ Adjustable

Annual Percentage Rate: ______
Term of Loan: 30 (years)
Number and dollar amount of monthly payments: 360 payments of $ 665.30

If an adjustable rate loan. maximum monthly payment $ __________

☐ Balloon payment:__________

No prepayment penalty

VI. ADDITIONAL LOAN TERMS

As we stated above and in connection with our comments on the GFE. we would delete this section and include all important loan terms in one location on page one of the form.

VII. Guaranteed Mortgage Package Agreement

We have suggested some technical revisions which appear in our revised form and which are intended to clarify that the agreement is subject only to verification of appraisal and income information submitted by the consumer and to a verification of a final credit report. These suggestions are intended to facilitate HUD's goal that this GMPA be a true guarantee and not be subject to bait and switch tactics. Neither the packager, nor any other party, such as a lender, should be able to impose new requirements after the GMPA is offered. Without such assurances, the integrity of the GMP system will be at significant risk.

GMP: Part II General Comments

Other Classes of Transactions That Should Be Excluded From the GMP: AARP welcomes HUD's inquiry into other classes of transactions which should not be deemed acceptable for GMP treatment and, by extension, eligible for the safe harbor from Section 8 liability. We commend HUD for denying the safe harbor to HOEPA loans and believe that the benefits of the GMP system in limiting liability should be restricted to those lending in the prime market.

AARP strongly supports the novel GMP concept its introduction and in the prime market. We believe that the prime market is a wonderful place to test this innovative GMP product. To the extent that kinks may need to be worked out, the proven competitiveness of the prime market will serve to illuminate any glitches in the system without adversely affecting consumers. However the subprime market is not as mature or competitive as the prime market. Many segments of the subprime market do not offer competitive products nor, typically, are consumers in that market effective comparison shoppers. In addition, virtually all of the predatory lending abuses occur in the subprime market and can even involve the deception of prime borrowers, who become saddled with expensive subprime loans. Currently, subprime borrowers have remedies under TILA and RESPA that can often be used either in litigation or in advance of litigation to restructure a transaction to benefit the consumer. It is imperative therefore, that necessary market conditions be created before existing legal remedies are weakened or removed.

AARP, HUD and many other groups are developing strategies to educate consumers on how to more proactively protect their own interests as they shop among the array of complex mortgage products and providers. The proposed revisions to the GFE, including the tight tolerances proposed by HUD, in conjunction with advances in education and expansion of the availability of counseling may, in time, compel greater competition These are two of the market requirements that must be developed to spur greater competition in the subprime market.

AARP is committed to working with the Department, industry and consumer groups to develop a competitive subprime market where consumers are offered the opportunity to comparison shop. AARP regards the following as indicators that a competitive subprime market is developing:

- Risk-based pricing, as evidenced by widespread availability of automated underwriting;
- Significant curtailment of predatory practices;
- Objective standards in the pricing of subprime loans, as opposed to opportunity pricing.

A waiver of Section 8 liability for subprime lenders by HUD under a GMP mortgage should be linked to the establishment of genuinely competitive conditions.

AARP believes the new proposal for the GFE will offer significant advantages to subprime borrowers over the current system without the corresponding risks of losing the ability to pursue RESPA and TILA rescission claims that will result from the GMP structure. These tradeoffs make sense for borrowers in the prime market where the opportunities for certainty and real competitive shopping may offset the loss of those protections. For borrowers in a market that has significant abuses, RESPA and TILA offer necessary remedies to save homes from foreclosure.

Until the subprime market has matured sufficiently to meet the indicia described above and subprime borrowers become better trained to shop effectively for mortgages, the GMP could have the perverse effect of disguising inflated costs and insulating abusive lenders, instead of the intended effect of reducing borrowers' costs. For example, a GMP might be offered to an unsuspecting consumer in which a $10,000 prepayment penalty (10 points) would be charged on a loan with a guaranteed settlement package of $8,000, that includes five lender points ($5,000) and an additional three points ($3,000) in closing costs. If financed into the principal of the loan, the consumer might well be unaware of the excessive pricing on this loan. Yet unlike the situation today, that consumer would lose the ability to challenge the allocation of fees to the amount financed, instead of the finance charge or to challenge inflated fees. Expensive loans, such as this one, are often accompanied by TILA violations that enable the consumer to save his/her home from foreclosure. With the GMP, the consumer would no longer have the information necessary to evaluate his/her TILA claims and to support a good faith claim for rescission.

AARP, therefore, recommends that the GMP be available only for loans in which the Guaranteed Mortgage Package Price is less than 5% of the principal of the loan.[2] See, AARP Model Home Protection Loan Act, §2(i); JOINT HUD-TREASURY REPORT ON RECOMMENDATIONS

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[2] We recommend that the cost of transfer taxes be excluded from this 5% calculation. It is important for borrowers shopping for a loan to understand that these taxes are part of the cost of the loan and, therefore, they should be included in the GMP. However, because the taxes vary significantly among jurisdictions and are outside of the packager's control, we recommend that they be excluded from the 5% calculation.

TO CURB PREDATORY HOME MORTGAGE LENDING, June 20, 2000, at page 11; Conduct of the Secondary Market Operations of the Federal National Mortgage Association. 24 C.F.R.§81.2; OTHER CITES. AARP encourages HUD to deny the safe harbor from Section 8 liability to any loans:

- Whose package price is equal to or exceeds 5% of the principal of the loan;
- With a prepayment penalty, or
- With lump sum insurance or insurance-like products[3] or debt cancellation products.

Given the difficulties of defining the absolute boundaries of predatory lending, and the importance of testing the GMP in a competitive marketplace, AARP believes this targeted group of mortgage loans should not be eligible for a safe harbor from Section 8 liability. We recommend that HUD study the impact and functioning of the GMP in the prime market over the next several years. It should be understood that nothing in AARP's proposal would prohibit subprime mortgage lenders from offering packages that guarantee interest rate and costs. Some lenders have been successfully offering this product in the prime market without receiving the exemption from Section 8 liability. Subprime lenders could take the same approach. Indeed, this might be an excellent proving ground for packaging in the subprime market. Establishing a track record of offering a guaranteed price and interest rate--and making good on that promise--will enhance the credibility of the subprime market such that an exemption from Section 8 liability would be justified.

Coordination of TILA and RESPA

AARP's support for the proposed GMP process is tempered by uncertainty about the treatment of the costs of the package under TILA. As HUD has noted, the implications of the GMP proposal extend far beyond the scope of RESPA and will impact disclosures required under TILA and HOEPA. Since the allocation of costs inside the package will be determined by the Federal Reserve Board after the proposed RESPA rule goes into effect, it is important that HUD coordinate with the Federal Reserve Board and that the public be afforded the opportunity to comment further on any proposed changes to Regulation Z or its Commentary.

Most important for HUD is that HUD retain the ability to identify loans that are ineligible for the GMP. HUD's proposal, which AARP strongly supports, would exclude all HOEPA loans from the GMP. Should the Federal Reserve Board adopt an "all in" rule that includes the entire GMP price in the finance charge, all parties who review the transaction would be readily able to determine whether a loan is covered by HOEPA. In contrast, if the Federal Reserve Board does not require the entire GMP price to be included in the finance charge, it will be virtually impossible to assess whether a loan is or is not subject to HOEPA. That is because the packaging and volume discounting that would be permitted by HUD's proposal would make it difficult, if not impossible, to accurately allocate costs to one service or provider versus another. Moreover, payments to affiliates who are in the package and who receive safe harbor from RESPA would need to be broken out as HOEPA points and fees to evaluate whether the loan is subject to

[3] Except for hazard insurance.

HOEPA. Again, this would be a difficult and unreliable task

The facts of every GMP transaction must be sufficiently transparent that HUD is in a position to enforce its regulation and police its safe harbor from Section 8 of RESPA. Neither HUD nor consumers will have enough information to regulate or police a GMP system where the GMP package price is not all in the finance charge. AARP's proposal offers a solution to this problem. By defining the bounds of the GMP:

< as a percentage of the principal of the loan,
< the absence of prepayment penalties, and
< the absence of lump sum insurance products,

AARP has offered HUD a transparent, sharply defined and enforceable safe harbor.

<u>Enforcement of the GMP</u>

<u>Failure to meet all requirements of the GMP must create a presumption of a violation of Section 8 of RESPA.</u>

A packager that offers and delivers on its promises of a guaranteed interest rate and package price will be exempt from liability under Section 8 of RESPA. In contrast, if packager fails to deliver on these promises, there must be presumption that it violated Section 8. The GMP offers a streamlined disclosure regime that does not require the itemization of costs. Absent a presumption, the borrower who does not receive the interest rate and package price promised would have to bear the impossible burden of proving the existence of an illegal referral or kickback with absolutely no information about the identity of the settlement service providers, what service each performed, and how much each was paid. Establishing a Section 8 violation is difficult under existing law. Absent a presumed violation for a failed attempt to package, kickbacks and referral fees will flourish with impunity.

<u>In addition to regulatory enforcement, class and individual relief under Section 8 must be available to ensure compliance with the GMP system</u>.

HUD has proposed that consumers be able to sue on a contract theory to enforce the GMP. AARP does not believe that the contract relief proposed by HUD, which would only return consumers to the deal they were promised in the first place, would have an impact sufficient to deter lenders and packagers from violating the GMP system. This is true even with the opportunity for class relief. It is critical that violation of the GMP system come with a sufficiently heavy penalty that packagers will have a strong incentive to deliver on the promises made in the GMP. The remedy afforded by Section 8 of RESPA, which awards treble damages, attorneys fees and costs creates such an incentive for compliance when accompanied by a class proceeding. AARP urges HUD to state explicitly that class relief is an important component of RESPA enforcement to ensure the integrity of the GMP system.

<u>GMP: Part III AARP Responses to Questions 11-21</u>

11. *Is a safe harbor along the lines proposed in Section III. C. (1) of this rule necessary to allow lump sum packages of settlement services to become available to borrowers?*

Some lenders are currently offering this product without a safe harbor. It may be necessary, however, to offer the safe harbor to encourage widespread marketing of a guaranteed rate and cost product. As long as the GMP is a *real* guarantee of interest rate, mortgage terms and settlement costs and is not available for HOEPA or other subprime loans, as discussed above, AARP supports the proposed safe harbor.

Would the proposed clarification by HUD that discounts may be arranged, if passed on to borrowers and not marked up, suffice to make packages available to borrowers?

AARP believes that the industry has long understood RESPA to permit "packaging" if volume discounts are passed on to borrowers. It does not appear that the proposed clarification would be sufficient to promote widespread packaging.

Would a rule change to approve volume discounts and/or mark-ups when a package is involved suffice?

This question is somewhat unclear. As AARP understands it, HUD is inquiring whether it should permit a safe harbor for a package without a guaranteed interest rate. As AARP has stated consistently throughout the mortgage reform process, such an exemption would be completely unacceptable. An exemption for packaging without a corresponding requirement to fix loan costs would simply allow lenders to game the system by shifting settlement costs into the interest rate on the loan. For example, a borrower might be offered a "guaranteed" package price of $500. If the lender later determined that it wanted to receive an additional $250 in profit or fees on the transaction, that could be easily achieved by slightly increasing the interest rate provided to the borrower. Since the borrower would not have been entitled to an interest rate guarantee, the lender would have been able to defeat the package guarantee, by recovering extra profit in the rate. Thus lenders and others would be relieved of significant liability under RESPA without providing a corresponding benefit to consumers.

Would it suffice to trim the disclosure requirements for packaging and offer the option of providing a streamlined GFE to those who packaged?

It is unclear what is being suggested here. If the suggestion is to offer a safe harbor for a streamlined, but not completely guaranteed GFE, we would oppose it. Only a completely guaranteed product, such as the GMP, removes the opportunity for an originator or packager to insert kickbacks into the pricing and inflate costs prior to closing.

12. *As proposed in Section III. C. (6), is the scope of the safe harbor appropriately bounded in applying to all packagers and participants in packages?* Yes.

The safe harbor also currently does not apply to referrals to the package. Should there also be a bar against part time employees of other providers working for the package to steer business? How should the safe harbor apply to affiliated business arrangements to protect borrowers from steering?

AARP understands this question to ask whether real estate brokers working for affiliates of packagers should be prohibited from steering to the affiliate's package. We would support HUD's continued prohibition on referral fees between these entities, but would not prohibit such a real estate broker from suggesting that a consumer obtain a GMP from an affiliated packager. We believe an affiliate is both appropriate and necessary in this situation.

13. *As proposed in Section III. C (5), to qualify for the safe harbor, the packager must include an interest rate guarantee with a means of assuring that when the rate floats, it reflects changes in the cost of funds not an increase in originator compensation. For this purpose, the rule suggests tying the rate to an observable index or other appropriate means. What other means could assure borrowers that the rate of a lender was not simply being increased to increase origination profits?*

We recommend that packagers be required to use an index that is readily available in the consumer's market area, preferably through a local newspaper. As we suggested in our comments, the packager should be required to identify where the consumer can locate the index and how the consumer can use the index to calculate the guaranteed rate.

For example, would a lender's commitment to constantly make rates public on a web site be a useful control?

We believe that there might be acceptable alternatives to use of an index to protect a consumer's guaranteed rate during the period prior to lock-in. For example, AARP would support a system in which packagers would precisely identify the product that forms the basis for the GMP offered to a consumer and inform the consumer how to locate that product on their product matrix. Under this system, the consumer would be entitled to receive the rate offered for that precise product whenever the consumer chose to lock in. The pricing information for that product must be easy for the consumer to locate (without the necessity of using a computer).

If an index is the best approach, how should it be set? If an index approach is approved, should each lender be allowed to pick its own observable index?

Consumer confusion would be minimized and comparison shopping facilitated by limiting the number of indexes that could be used in a particular marketplace. It is also critical that the packager provide clear instructions to enable consumers to calculate daily changes in their guaranteed rate based on movement in the index.

14. *As discussed in the preamble to the rule in Section III. C (5), if an observable index or other appropriate means of protecting borrowers from increases in lender compensation when the borrower floats in a guaranteed packaging approach is not practical, should HUD provide a packaging safe harbor only for mortgage brokers?*

No. We believe that a rate guarantee based on an observable index or some other readily identifiable matrix or system of published rates is workable and practical. AARP does not believe that a packaging-only safe harbor is a workable solution for either a lender or a brokered transaction. As we commented earlier, it is essential that borrowers be provided both a closing cost or package guarantee *and* an interest rate guarantee as a prerequisite for offering a safe harbor.

Such a mortgage broker safe harbor would require disclosing the lender credit to the borrower in broker guaranteed packages. The theory for the safe harbor would be that any amounts in indirect fees could be credited to borrowers taking away any incentive for an increase in rates to increase compensation. Should this be offered in any event?

No. This simply doesn't offer a benefit to consumers that is sufficient to justify the loss of Section 8 protection. AARP has taken the position consistently that a safe harbor for mortgage brokers is possible only when the consumer can direct how the mortgage compensation is to be paid and is offered several choices of guaranteed interest rate and closing costs. This proposal, which would enable mortgage brokers to increase their compensation as long as it was disclosed, would merely serve to validate mortgage broker gouging, by removing the Section 8 remedy. Disclosure is no substitute for substantive protection.

15. *As proposed in Section III. C (6), under the rule, mortgages with total fees or a rate covered by the Home Ownership and Equity Protection Act (HOEPA) would be subject to the new GFE disclosure requirements; however, HOEPA loans would not qualify for the guaranteed package safe harbor. Is this exclusion appropriate considering, on the one hand, that packaging promises borrowers a simpler way to shop and make transactions more transparent?*

Yes. To the extent that lenders choose to make HOEPA loans, borrowers should be able to evaluate each of the fees charged, etc. A safe harbor should not be permitted for those loans whose interest rate or fees are so high that they reach the HOEPA triggers. These borrowers are the most vulnerable and the least likely to benefit from opportunities to shop. HOEPA lenders should not be permitted to benefit from the special exemption afforded by the safe harbor.

On the other hand, the safe harbor could be provided for a loan that has very high rate and/or fees and may be predatory. The proposal also says that during the rulemaking other limitations may be established to exclude high cost and/or loans with predatory features from the packaging provisions. HUD invites comments on whether HOEPA loans, any other loans, or features of loans should be included or excluded from the safe harbor and why.

See AARP's comments in GMP: Part II above for a discussion of additional exclusions from the safe harbor.

16. *As proposed in Section III. C (3), the GMPA provides that the offer must be open to the borrower for at least 30 days from when the document is delivered or mailed to the borrower. Is this an appropriate minimum time period to ensure that the borrower has an adequate opportunity to shop?* Yes.

17. *As proposed in Section III. C (4), the rule currently provides that the Guaranteed Mortgage Package agreement must indicate that certain reports such as the appraisal, credit report, and pest inspection are available to the borrower upon the borrower's request. Also, packagers may decide to forego such reports or services (i.e. lender's title insurance) and must inform the borrower that such reports or services are not anticipated to be included in the package price. Are these adequate protections for the borrower? HUD is aware that other laws such as Regulation B (ECOA) provide certain rights to borrowers with respect to obtaining some of these reports. In order to qualify for the safe harbor HUD has created additional reporting requirements. Are these additional reporting requirements appropriate?* Yes.

18. *Should additional consumer protections be established for packaging? For example, should additional qualifications be established for "packagers" to ensure that borrowers are protected against non-performance including the unavailability of a mortgage that could result in a borrower "losing" a house? For example, should there be a requirement that a packager must have sufficient financial resources to credibly back the guarantee?*

AARP believes that additional consumer protections should be required for packaging. Packagers will be getting a significant benefit from the waiver of Section 8 liability. In exchange for that benefit, consumers must have the assurance that the packagers can and will perform. It would completely undermine the new GMP scheme if, after shopping and selecting a package, the consumer is left in the lurch without a loan simply because the packager has made a GMP offer which it cannot deliver. HUD should impose requirements, such as capital requirements, to assure that the GMP system works for consumers.

Is it necessary to require a lender signature on the GMPA to ensure that the borrower receives the loan at the time of settlement?

This is absolutely necessary to ensure that the borrower will be able to receive the promised loan. In the event that a packager is unable to deliver on a promised package, a borrower will learn this early on and be able to turn to one of the other alternative packages that was offered. In fact, AARP suggests that a better approach would require the lender to sign on at the time the GMP is offered. This would provide the greatest level of assurance that the package had the backing of a lender.

Should HUD decide not to require a lender signature at all, many consumers might discover at settlement that their loan will not be delivered. That would place those consumers in a very precarious position and could result in their agreeing to unfavorable loan terms, since most consumers will not have the freedom to walk away from the transaction.

How can the borrower's interests be protected without unduly burdening the process or unduly limiting the universe of packager(s)?

AARP does not believe that the process will be unduly limited or that the universe of packagers will be unnecessarily constricted by adopting the above suggestions.

19. *Consistent with the HUD-Fed Report, the rule proposes that certain charges, such as hazard insurance and reserves, are outside the package as other or optional costs. Is this the right approach or should these charges be disclosed as the minimum amounts required by the lender and required to be inside the package? Would the latter better serve the objective of establishing a single figure for the borrower to shop with?*

The current approach is acceptable, especially given the current market practice in which consumers generally arrange their own hazard insurance.

20. *The rule proposes in Section III. C (3), that under Guaranteed Mortgage Packaging, the HUD-1 will list the settlement services in the package but not the specific charges for each service. Certain third party charges are excluded from the calculation of the finance charge and the APR under TILA and HOEPA. Commenters are invited to express their views on whether the approach in the rule satisfies or whether alternative approaches to cost disclosures should be established to ensure consumers' rights under TILA and HOEPA while facilitating packaging. More broadly, commenters are invited to provide their views on means of better coordinating RESPA and TILA disclosures.*

AARP has commented on this issue in the discussion above.

21. *Commenters are asked to provide their views on how the rules should treat mortgage insurance? The rule proposes in Section III. C (3), that the guaranteed package would include any mortgage insurance premiums in the APR and up-front costs of mortgage insurance in the guaranteed package. "Other Required Costs" would include reserves for mortgage insurance premiums. However, because the packager will not have an appraisal at the time the GMPA is provided, the packager may not have firm information to provide a definite figure. Another possibility is to exclude mortgage insurance from the package but notify the borrower that mortgage insurance may be an "Other Required Costs" and present the borrower an estimate subject to a tolerance, if mortgage insurance is necessary. This approach would exclude a major charge from the package. HUD recognizes that there are state laws that prohibit rebates or any splitting of commissions for mortgage insurance. How, if at all, should this impact the decision to include mortgage insurance in packages of settlement services?*

The packager must be able to rely on the consumer's assessment of the value of the home for purposes of calculating whether or not mortgage insurance will be required and the amount that will be required as a component of the monthly payment and as an escrow reserve. As we have stated above and as we have included in AARP's proposed revisions to the GMPA, the consumer's valuation of the house must be a stated premise of the GMPA and the amount of mortgage insurance included in the GMP price offered to the consumer. Therefore, this should not be an issue of concern to HUD. To the extent that the consumer's valuation supports the need for mortgage insurance, it should be included as a component of the GMP price and should not be excluded from the package. AARP agrees with HUD that excluding mortgage insurance from the GMP price would, for many consumers, undermine the value of receiving the guaranteed package price.

AARP COMMENTS ON OTHER TOPICS RELATING TO THE GFE AND GMP

Other Topics Relating to the GFE and GSE: Part I

Disclosure of Affiliate Relationship on the HUD-1 Settlement Statement

AARP suggests that this rulemaking is an ideal time to clarify an issue that has been outstanding since the passage of HOEPA in 1994. HOEPA created duties and liabilities for lenders that did not exist previously. Under HOEPA, any charge on the HUD-1 that is paid to the lender or to an affiliate of the lender is countable toward HOEPA's points and fees trigger. 15 U.S.C.§1602(aa); Reg. Z, 12 C.F.R. §226.32(b). However, there has been no amendment to Regulation X to facilitate the enforcement of this provision of HOEPA. In fact, AARP attorneys have encountered countless situations where payees for charges paid by the elderly homeowners are not identified on the HUD-1. While it was always important to be able to identify the payee on a HUD-1, HOEPA has made the identity of the payee and a determination of the payee's relationship to the lender a legal necessity. Identification of affiliates has also become a legal necessity under the many of anti-predatory lending laws passed by the states.

AARP urges HUD to adopt amendments to Regulation X to require not only that payees be named on each line of the HUD-1, but also that the each line indicate whether or not the payee is an affiliate of the lender. If the payee is not named, or the affiliation not specified, Regulation X should create a presumption that the payee was the lender or an affiliate of the lender.

Lock-in and Other Miscellaneous Fees

AARP is concerned that HUD has not provided direction to packagers and providers of GFEs as to the permissible treatment of lock-in fees and other miscellaneous costs that a lender or other provider may seek to impose on borrowers at or before settlement. HUD has not indicated whether a separate lock-in fee will be permitted to be charged in a GMP loan or whether such a fee must be included in the package. AARP believes that a lock-in fee is a cost of the loan and should be included as a component of the GMP price. HUD must make it clear that miscellaneous fees, such as lock-in fees, courier fees, etc., that arise at a later time in the transaction may not be added to the borrower's costs without violating the safe harbor. To the extent that lenders are permitted to charge add-on fees after the borrower has shopped for the loan, they will be defeating the purpose of the GMP.

Similarly, a lock-in fee would have to be included in the GFE at the time it is issued as a component of total origination fees. To permit later imposition of such a charge would defeat the "zero tolerance" rule proposed by HUD. Miscellaneous services, such as courier fees, should also be included up front at the time the GFE is presented to the consumer and should not be permitted to be added to settlement costs at a later date.

Other Topics Relating to the GFE and GSE: Part II AARP Responses to Questions 22-30

22. *To what extent, if any, do inconsistencies currently exist, or would they exist upon promulgation of the proposed rule between State laws and RESPA? Specifically, what types of State laws result in such inconsistencies and merit preemption? What, if any, provisions of the proposal should be revised to facilitate any necessary preemption?*

AARP encourages HUD to conduct an extensive evaluation of state laws that might be impacted by the new rule and to consult with state regulators. We believe it is important to minimize the degree of preemption to the greatest extent possible to honor the legislative and regulatory choices of the states to protect their consumer/citizens. This is especially true regarding the many anti-predatory lending laws and regulations enacted in recent years. AARP supported many of these state efforts, which, in most instances, offer significant, substantive protections and remedies against predatory lending. While the proposed regulation offers some consumer benefits, it does not, as the Secretary has clearly recognized, purport to address the problem of predatory lending. HUD should take great care that use of its preemption authority not exacerbate predatory lending abuses. AARP strongly opposes the use of this new regulation to preempt these state laws.

23. *The rule proposes that the GFE and GMPA be given subject to appraisal and underwriting. How should the final rule address the matter of loan rejection or threatened rejection as a means of allowing the originator to change the GFE or GMPA to simply earn a higher profit?*

AARP believes that HUD must impose a record keeping requirement so that borrowers (or HUD) can prove that an originator has changed the deal. Unless the originator/packager is required to retain copies of all GMPs/GFEs, at least for the loans it has closed, for some extended period of time (for example, three years), borrowers/HUD will not be able to prove that this unacceptable behavior occurred. In addition, a record keeping requirement will assist in preventing the originators from gaming the system by offering multiple GMPs/GFEs to a borrower.
To the extent that originators/packagers try to bait and switch borrowers or extort a higher fee, we recommend that this behavior be explicitly described in the regulation as an unfair practice that is actionable under appropriate state and federal laws.

24. *To what extent, if any, should direct loan programs such as those provided by the Rural Housing Service of the Department of Agriculture be treated differently under the new regulatory requirements proposed by this rule?*

AARP has no comment.

25. *As proposed, the GFE and GMPA currently contain sections for loan originators and packagers to indicate the specific loan terms for adjustable rate mortgages, prepayment penalties, and balloon payments. Are these appropriate loan terms to include on these forms and what, if any, other mortgage terms or conditions should be listed on the forms?*

These are absolutely appropriate terms and are essential to enable the consumer to shop and compare mortgage products. However, they should be grouped together with the other loan terms, preferably in a prominent box on the first page of the form. (See above).

Balloon term: As currently placed on a separate page of the disclosure, far from other loan terms, a consumer might not realize that a balloon is a component of his/her loan. For example, under the current proposal, the loan terms on page one of the GFE or GMPA might disclose the loan as being at 7.5% interest, 7.8% APR, for a 180 months with a monthly payment of $______. This would appear to be an amortizing 15 year loan. If in fact, the loan is not fully amortizing, but requires a balloon payment at the end of the loan term, that important information should be disclosed in the same location as the other loan terms. The current placement of the balloon term on a different page could lead to significant confusion, if not outright deception. The absence or presence of a balloon payment is a key feature of the loan product and should not be buried on page 2. In fact, in AARP's experience, borrowers are frequently deceived into believing that a loan is fully amortizing and are surprised to learn about the balloon feature of their mortgage loan. For this reason, it is key to place that information with other loan terms.

Term of the loan: AARP believes that it is useful to identify the loan term in years, not just in number of payments, as that is how most consumers and lenders identify different loan products, i.e. 30 year fixed rate loan; 15 year balloon loan.

Prepayment penalty: The existence and maximum cost of a prepayment penalty is a significant factor that a consumer should consider in comparing loan products. It is not enough to disclose the existence or non-existence of a prepayment penalty and to do it in a location remote from other key loan terms. The maximum cost of the penalty should also be disclosed and in the same location as key loan terms. A loan which appears to charge only minimal out-of-pocket costs, but which carries an expensive (6 points) prepayment penalty will be less desirable to many consumers who wish to be able to refinance or sell their homes during the prepayment period. However, a small prepayment penalty of perhaps 1% for 1 year may not be an obstacle to many consumers. There is simply no reason to withhold this information, which is essential to intelligent comparison shopping. Since prepayment penalties are often features of predatory loans and infrequently components of prime loans, it is important to provide prominent notice of their inclusion in the loan. In addition, for that reason, AARP has recommended that the GMP should not be available for loan products that contain a prepayment penalty. (See above). Nevertheless, to enable consumers who are offered a GMP by some originators and a GFE by others to comparison shop, AARP recommends that the loan terms in the GMP clearly indicate: "no prepayment penalty."

Adjustable interest rates: In AARP's experience, many consumers with adjustable rate loans are unaware that the rate can adjust until the first adjustment occurs. As with the balloon information, a consumer could easily be misled or deceived by the placement of the adjustable rate information on page 2 of the forms. Moreover, AARP believes that the information most useful to consumers is the maximum possible monthly payment that could be charged on the loan, which can be easily added to the mortgage terms on page 1. Including the maximum monthly payment will enable consumers to evaluate the risk in taking on an adjustable rate loan and to compare differences among different adjustable rate products. We do not believe that it is as helpful to consumers to provide the other more detailed information, such as maximum APR, that HUD has proposed to include on p. 2. We would include only the initial rate and payment and the maximum payment and would place them together on page 1 of the GFE or GMPA.

Default interest rates: HUD might wish to include a disclosure of default interest rates which exceed the *note rate* as an item identified on the GMPA and GFE. If HUD adopts AARP's proposal that the GMP be limited to the prime market, this disclosure may not be necessary.

26. *What are the arguments for and against limiting the proposed rule to purchase money, first and second lien, and refinancing loans as opposed to offering it to home equity, reverse mortgage and other transactions? Should there be any additional requirements for so-called B, C, and D loans?*

AARP strongly supports expanding the requirement for a GFE to open-ended loans. *See AARP Model Home Loan Protection Act.* When these loans were first created, they did not involve significant upfront costs. As a result, they were not thought to require the regulation imposed in the closed-ended loans. This is no longer the case. As HUD and the Federal Reserve Board have recognized, there are serious abuses across the country with spurious open-ended loans. The home equity line loophole needs to be closed so that consumers will be in better position to understand early on the costs involved in these loans.

AARP would also support providing the benefits of a new GFE to reverse mortgage borrowers. Fixing the charges imposed by the lender and broker early in the process would facilitate shopping and predictability. But reverse mortgage terms and costs are so different from those of "forward" home loans that using a "one size fits all" GFE form for both types of mortgages is very likely to mislead consumers who are considering reverse mortgages. Therefore, AARP recommends that HUD propose a separate GFE for reverse mortgages that takes into account the unique features of these loans.

For example, a GFE for reverse mortgages should include more detail on the mortgage amount. Specifically, it should indicate any amount to be provided to the borrower as a lump sum at closing, as a monthly loan advance for a fixed or open-ended term (including the length of any fixed term or a description of any open-ended term), or as a line of credit (including any rate by which the amount of available credit will initially increase over time, whether this rate is fixed or adjustable, and for how long such increases will apply).

For the majority of reverse mortgages, which do not have a fixed term to maturity, the GFE should include a checklist of events that can lead to default or acceleration of the loan, or otherwise require loan repayment. On the other hand, the GFE should not include information on the number and dollar amounts of monthly loan repayments, as none are required on reverse mortgages.

All reverse mortgages require a balloon payment at loan maturity. But the amount of the payment depends on the amount of the initial charges added to the loan balance, the timing and amount of any subsequent periodic loan charges, the loan advances made to the borrower during the loan term, the interest rate charged on all of these items, and the value of the home at loan maturity. (The home's future value can be a key determinant of the terminal loan balance because reverse mortgages are non-recourse loans, which means that the loan balance cannot exceed the home's value at maturity.)

Requiring a single balloon payment figure, therefore, would make little sense. Instead, as discussed below, the GFE should require a loan projection that shows how this figure depends on when the loan is repaid.

The non-interest costs of a reverse mortgage are typically not limited to settlement costs, that is, some of them are charged on a periodic basis throughout the loan. For example, on the federally-insured Home Equity Conversion Mortgage (HECM), which accounts for over 90% of all reverse mortgages currently being closed, a flat servicing fee is charged and added to the loan balance on a monthly basis. In addition, part of the loan's mortgage insurance premium (MIP) is charged on a monthly basis as a percent of the loan's then current balance.

Other reverse mortgages have charged "contingent" interest at loan maturity that depends on the home's value at the time, or on any increases in the home's value since origination. Although most of these "shared equity" and "shared appreciation" reverse mortgages are no longer being offered, at least one is still being marketed, and others could be developed.

Periodic and contingent charges mean that the cost of these loans cannot be adequately portrayed by disclosing the interest rate and settlement costs alone. That is why the Congress amended TILA to require a specialized cost disclosure for reverse mortgages that combines all of its costs, including those not required to be included in APR calculations, into a single rate. In effect, the Total Annual Loan

Cost (TALC) rate is the interest rate a lender would charge if all of the loan's costs had to be included within it.

This TALC disclosure reveals that the true, total cost of these loans depends significantly on three factors other than interest and loan costs: how long consumers live in their homes, what happens to their homes' value during that time, and the timing and amount of the loan advances they request from the lender. Due primarily to these factors, it is virtually impossible for two reverse mortgages that have identical known costs at closing to cost the same when they are repaid. TALC disclosures also demonstrate that the difference in total cost between two such loans can be significantly greater than the cost difference between two highly dissimilar "forward" mortgages.

Although they are not required to do so, reverse mortgage lenders typically provide the TALC disclosure at the time of the GFE. They typically also provide a year-by-year projection that shows consumers how much principal they will have received, how much they will owe, and how much equity they would retain at the end of each future year.

To bring some uniformity to these projections, AARP invited consumer and industry interests to develop consensus model specifications for analyzing and comparing reverse mortgages. As a result, leading reverse mortgage industry interests initiated efforts to create software that meets these specifications. One application is currently in widespread use, and others are expected to be released. Independent nonprofit counselors who use this software give it high marks for explaining and comparing these loans.

When the true benefit and total cost of a mortgage product depends significantly on non-cost factors that are indeterminate at closing, this type of year-by-year loan projection provides a helpful benchmark for potential borrowers. It projects their total cash benefit, total cost, and remaining equity on a year-by-year basis. Projections meeting the consensus model specifications also give consumers an individually-customized total cost rate that takes into account how they intend to use a reverse mortgage creditline, which by a wide margin is the loan advance plan most frequently selected by reverse mortgage borrowers. This feature represents an important advance over TALC methodology, which assumes that all creditline borrowers use 50% of their available credit at closing and none thereafter.

Consumers who want to compare a federally-insured HECM to some other reverse mortgage need these projections, primarily because the amount of the loan advances available through a HECM versus other products is likely to be substantial. This often sizeable discrepancy in loan amount makes it virtually impossible to compare these loans without a technically sound, side-by-side comparison of projected total benefits, total costs, remaining equity, and an individually-customized total cost rate.

But for the vast majority of consumers, for whom the HECM program clearly provides the best value, a much simpler GFE could be very helpful. In proposing a GFE for reverse mortgages, however, HUD should also consider that trade-offs between interest rates and settlement or other costs are rarely, if ever, offered in this market.

Regarding the GMP, AARP believes testing the GMP system in the forward mortgage market may provide helpful insights for its potential application to reverse mortgages. In the future, a GMP could be beneficial to reverse mortgage borrowers, but it would have to be structured to take into account the issues discussed above.

And discussed above, AARP proposes that the GMP not be available for several categories of loans which might also be referred to as B, C and D loans until the market becomes competitive. These categories would include:

- loans with a GMP price equal to or greater than 5% of principal of loan;
- loans containing prepayment penalties;
- loans charging lump sum credit insurance and analogous products.

27. *As proposed, the Guaranteed Mortgage Package includes one fee for settlement services required to complete a mortgage loan. The fee for the package will include loan origination fees, typically referred to as "points." As points are generally deductible under IRS rules, comments are invited as to how to determine which portion of the package prices should be deemed to constitute points.*

AARP has no comment.

28. *To what extent do the proposed changes to the definition of application in Section III. B (2) a., and requirements for delivery of the GFE impact other federal disclosure requirements, such as those mandated by the Truth in Lending Act? How can the disclosure objectives of the proposed rule be harmonized with such other disclosure requirements?*

We recommend that HUD coordinate with the Federal Reserve Board on the timing and coordination of these disclosures. To the extent that the Board proposes to change existing timing requirements, we would hope to have the opportunity to comment on such proposed changes.

29. *The proposed rule in Section III. B (2) c., would require a loan originator capable of offering an alternative loan product to provide a prospective borrower, upon the borrower's request, with a new GFE if, after full underwriting, the borrower does not qualify for the loan identified on the original GFE. Is this approach appropriate? What other options should be considered where borrowers do not qualify for the loan product initially sought?*

AARP believes HUD's rule in this area should track the requirements of the Equal Credit Opportunity Act.

30. *The proposed rule in Section III. B (2) c., would require loan originators to provide qualified borrowers with an amended GFE, identifying any changes in costs associated with changes in the interest rate, where the borrower elects not to lock-in the interest rate quoted on the original GFE at the time it is provided. Is this an appropriate requirement? What alternatives, if any, should HUD consider?*

AARP believes that the new rule should be structured so that lenders cannot issue amended GFEs. Amended GFEs simply create the opportunity for bait and switch. AARP believes that amendments would not be necessary if HUD were to adopt our proposal that a 10% tolerance apply to all categories of settlement charges, other than lender and broker origination fees. In the absence of very unusual, large swings in the mortgage market during the shopping period, this 10% tolerance should cover any normal variation in the interest rate. Even in this rare case, it would be preferable not to amend the GFE. Instead, to the extent that HUD wishes to provide more certainty at the time the interest rate is fixed, HUD could permit or require the originator to attach to the original GFE, an amended disclosure of the "Other Charges" category and show how the "locked-in" rate changed the per diem interest component of that category of charges. Similarly, to the extent that HUD contemplates disclosure of other changes to the information provided in the original GFE, AARP strongly recommends that any such changes be disclosed on documents attached to the original GFE and that the original GFE not be discarded.

CONCLUSION

AARP commends HUD for undertaking the very complex and often polarizing issues of mortgage reform. HUD has proposed a comprehensive and innovative approach to educating consumers about the functioning of the mortgage market, promoting comparison shopping and ensuring certainty about the settlement costs and pricing of home mortgages.

AARP pledges to continue its ongoing relationship with HUD to work through the details of this proposal and to ensure that it becomes a reality and provides new and much needed products to promote American homeownership.

Sincerely,

Christopher W. Hansen
Director of Advocacy

Good Faith Estimate of Settlement Costs (GFE)   **Appendix I AARP revised GFE**

This form provides a reliable estimate of the funds that will be required from you, ______________________, the borrower(s) to obtain a mortgage using our company as your loan originator. This GFE covers both our charges, the charges of other settlement service providers who perform services that are required by the lender to close your mortgage loan, and applicable State and local government charges and taxes due at settlement.

The following estimate is valid for _____ days [30 days or greater] from the date this form is delivered or mailed to you, if you qualify for this mortgage based on your credit rating, the appraisal, and other appropriate criteria.

THE PROPERTY: You seek to [purchase][refinance] a residential property at (Address)____

I. YOU SHOULD COMPARE THE PRICES IN THE BOXES BELOW AND SHOP FOR THE LOAN ORIGINATOR, MORTGAGE PRODUCT, AND SETTLEMENT SERVICES THAT BEST MEET YOUR FINANCING NEEDS.

===

II. ESTIMATED LOAN TERMS:

Mortgage Amount: ___________
Interest Rate: ___________
- ☐ Fixed
- ☐ Adjustable

Term of Loan:___________ (years)
Number and dollar amount of monthly payments____________
including:
- ☐ principal
- ☐ interest
- ☐ mortgage insurance
- ☐ real estate taxes
- ☐ hazard insurance

If an adjustable rate loan, maximum monthly payment $ _________
- ☐ Balloon payment:__________
- ☐ Maximum prepayment penalty $__________

===

III. SETTLEMENT COSTS:

A.	**Net Charges by Broker and Lender**		$500
	1. Lender and Broker Charges (owed by borrower)	$2,000	
	2. Payments Based on Your Interest Rate		
	(a) Additional amount borrower will pay toward **Charges** (reduces interest rate)	+ $0	
	(b) Amount lender will pay toward **Charges** (Because of increased interest rate)	-$1,500	
		$ 500	
B.	**Title and Settlement Services**		$1,500
C.	**Other Necessary Charges**		$500
	Net Settlement Costs Due From Borrower (cash to close)		$2,500

OPTIONS TO PAY SETTLEMENT COSTS AND LOWER YOUR INTEREST RATE-
GFE page 2

A. Cash Payment at Settlement: You may pay all or part of your required settlement costs at settlement using your available funds.

B. Borrowing Additional Funds to Pay Settlement Costs: You may be able to pay all or part of your settlement costs by borrowing the needed funds as part of your mortgage loan principal. If you chose this option, your monthly payments will increase.

C. Pay Settlement Costs Through a Higher Interest Rate.
You may be able to lower your settlement costs in exchange for paying a higher interest rate on your mortgage loan. This higher interest rate will increase your monthly payments.

D. You May Lower Your Interest Rate:
You may be able to lower the interest rate on your loan by paying additional funds at closing, commonly referred to as "discount point." The reduced interest rate will lower your monthly payments.

Your loan will cost $2,000 in Charges by Broker and Lender and an additional $2,000 in Settlement costs for a total of $4,000. You have several choices about how to pay for these costs.

Choice #1-- Lender will pay $1,500 toward the Charges by Broker and Lender
You will pay a total of $2,500 at closing:
$500 for Charges by Broker and Lender,
+ $2,000 for settlement costs at closing.

Loan terms of:
(same as choice on page 1)
Mortgage Amount: $100,000
Interest Rate: 7 %
☐ Fixed √
☐ Adjustable
Term of Loan: 30 (years)
Number and dollar amount of monthly payments: 360 payments of $ 665.30
If an adjustable rate loan, maximum monthly payment $ ________
☐ Balloon payment:$ 0
☐ Maximum prepayment penalty $ 0

Choice #2 - Lender will pay $2,500 toward the Charges by Broker and Lender
You will pay a total of $1,500 at closing:
-$500 for Charges by Broker and Lender,
+ $1,500 for settlement costs at closing.
Loan terms of:

Mortgage Amount: $100,000
Interest Rate: 7.25 %
☐ Fixed √
☐ Adjustable
Term of Loan: 30 (years)
Number and dollar amount of monthly payments: 360 payments of $ 682.18
If an adjustable rate loan, maximum monthly payment $ ________
☐ Balloon payment:________
☐ Maximum prepayment penalty $ 0

Choice #3 -- Lender will pay $ 0 toward the Charges by Broker and Lender
You will pay a total of $4,000 at closing:
$2,000 for Charges by Broker and Lender,
+ $2,000 for settlement costs at closing.
Loan terms of:

Mortgage Amount: $ 100,000
Interest Rate: 6.25 %
☐ Fixed √
☐ Adjustable
Term of Loan: 30 (years)
Number and dollar amount of monthly payments: 360 payments of $ 615.72
If an adjustable rate loan, maximum monthly payment $ ________
☐ Balloon payment:________
☐ Maximum prepayment penalty $ 1,500.

Guaranteed Mortgage Package Agreement (GMPA)   Appendix II AARP revised GMPA

This GUARANTEED MORTGAGE PACKAGE AGREEMENT commits us, ____________ the PACKAGER, to provide you, ____________, the BORROWER(S), upon your acceptance and payment of a $____ fee within ____ days (30 days or greater) of the date this form is delivered or mailed to you:

- a mortgage loan on the property described below at a GUARANTEED INTEREST RATE;
- a GUARANTEED MORTGAGE PACKAGE PRICE for settlement services required by the lender;
- a firm estimate (within 10%) of the amount of OTHER REQUIRED SETTLEMENT COSTS you will pay at or before settlement; and
- the TOTAL ESTIMATED SETTLEMENT COSTS that you will be required to pay at or before settlement to obtain your mortgage.

The guarantees offered in this Guaranteed Mortgage Package Agreement are based on:

- you (the borrower(s)') statements that your gross monthly income is $____ and that the value of the home you seek to [purchase][refinance] located at ____________ is $____; and
- on a credit analysis performed by the Packager. This Agreement is subject to final verification of your credit rating, the value of the property, and your income and other information provided by you.

YOU SHOULD SHOP TO FIND THE BEST MORTGAGE PRODUCT TO MEET YOUR NEEDS.

I. INTEREST RATE GUARANTEE: We guarantee to provide you with a loan on the following terms:

Mortgage Amount: $100,000
Interest Rate: 6.75%
- ■ Fixed
- ☐ Adjustable

Annual Percentage Rate:________
Term of Loan: 30 (years)
Number and dollar amount of monthly payments 360 payments of $ 648.60
the monthly payment includes payments only for those items that are checked:
- ■ principal
- ■ interest
- ☐ mortgage insurance
- ☐ real estate taxes
- ☐ hazard insurance

If an adjustable rate loan, maximum monthly payment $ ________
☐ Balloon payment: $________
No prepayment penalty

☐ The interest rate is guaranteed through settlement if you accept and sign this agreement now and lock-in the rate by ________[date/time].

☐ If you accept and sign this agreement by _____ [30 days or more], we guarantee that the interest rate will not exceed ___ over _____[index] rate at the time of lock-in. [60 days or lender's time limit on lock-in]. You can easily check your rate by locating the index ________[where] and doing the following calculation:____________.

☐ [Alternative language] The loan product we have offered you is our ____ product. If you accept and sign this agreement by ______ [30 days or more], we guarantee that you will receive the interest rate that we are offering to our customers for our ___ loan product [same product as that identified above] at the time you lock in [60 days or lender's time limit on lock-in]. You can easily check those rates by ________.

If you do not accept by ________, this offer will expire.

I. GUARANTEED MORTGAGE PACKAGE

This is a GUARANTEED MORTGAGE PACKAGE PRICE for all settlement services and charges required by the lender to complete your mortgage. The precise services for each transaction may vary. *(See Attachment A-1 for an indication of whether we anticipate pest inspection, lender's title insurance and property appraisal services being included in your guaranteed mortgage package.)*

This guaranteed mortgage package price may include a mortgage insurance premium. The mortgage insurance premium may decrease or be removed after full underwriting.

GUARANTEED MORTGAGE PACKAGE PRICE: $ 1,500

II. OTHER REQUIRED SETTLEMENT COSTS:

You may be required to pay advanced mortgage and hazard insurance premiums, and to establish escrow reserves at settlement. Some of these costs may vary depending on when your loan closes and how much insurance you are required to obtain. **No cost my be imposed on you at settlement that is not specifically itemized and estimated in this Section other than the Guaranteed Mortgage Package Price.**

A.	**Per Diem Interest (daily interest)** Per Diem at $ 10 @ 10 days with an estimated Settlement date of ______.	+	$ 100
B.	**Reserves/Escrow**, (if required)	+	$ 1,200
C.	**Hazard Insurance**	+	$ 700
III.	OPTIONAL OWNER'S TITLE INSURANCE	+	$ 0
	TOTAL SETTLEMENT COSTS (GMP + other + optional)	=	$ 3,500

OPTIONS TO PAY SETTLEMENT COSTS AND LOWER YOUR INTEREST RATE-GMPA page 2

A. Cash Payment at Settlement: You may pay all or part of your required settlement costs at settlement using your available funds.
B. Borrowing Additional Funds to Pay Settlement Costs: You may be able to pay all or part of your settlement costs by borrowing the needed funds as part of your mortgage loan principal. If you chose this option, your monthly payments will increase.
C. Pay Settlement Costs Through a Higher Interest Rate:
You may be able to lower your settlement costs in exchange for paying a higher interest rate on your mortgage loan. This higher interest rate will increase your monthly payments. For every rate increase of 1/8, you can reduce your cash payment by $500. You can increase your rate up to ½ point to reduce your cash payment by a maximum of $2,000.
D. You May Lower Your Interest Rate:
You may be able to lower the interest rate on your loan by paying additional funds at closing, commonly referred to as "discount point." The reduced interest rate will lower your monthly payments. You may buy the rate down by paying $500 for every 1/8 point buydown up to a maximum of ½ point and $2,000.

Choice #1-- GMP: $1,500 + other required services: $2,000 = $3,500 cash to close
(same as choice on page 1)
Loan terms of:
Mortgage Amount: $100,000
Interest Rate: 6.75 %
☐ Fixed √
☐ Adjustable
Term of Loan: 30 (years)
Number and dollar amount of monthly payments: 360 payments of $ 648.60
If an adjustable rate loan, maximum monthly payment $ _________
☐ Balloon payment:$ 0
No prepayment penalty

Choice #2 - GMP: $1,500 + other required services: $2,000 = $3,500 minus $1,000 to increase interest rate by 1/4 point = $2,500 cash to close

Loan terms of:
Mortgage Amount: $100,000
Interest Rate: 7 %
☐ Fixed √
☐ Adjustable
Term of Loan: 30 (years)
Number and dollar amount of monthly payments: 360 payments of $ 665.30
If an adjustable rate loan, maximum monthly payment $ _________
☐ Balloon payment:__________
No prepayment penalty

Choice #3 -- GMP: $1,500 + other required services: $2,000 = $3,500 plus $1,000 to reduce interest rate by 1/4 point = $4,500 cash to close

Loan terms of:
Mortgage Amount: $ 100,000
Interest Rate: 6.5 %
☐ Fixed √
☐ Adjustable
Term of Loan: 30 (years)
Number and dollar amount of monthly payments: 360 payments of $ 632.07
If an adjustable rate loan, maximum monthly payment $ _________
☐ Balloon payment:__________
No prepayment penalty

===

VII. Guaranteed Mortgage Package Agreement:

We are providing this GMPA to you at no cost. If you agree to seek a mortgage loan using our services within 30 days, by signing, dating, and returning this GMPA to us on or before ____________, along with a $_______ application fee, we will be contractually bound to the terms of this GMPA provided that you continue to qualify for this mortgage based on your credit rating, and verification of the appraisal, and other income information.

Signature of Authorized Agent   Date   Signature of Lender   Date

Signature(s) of Borrower(s)   Date

Testimony

Before

THE SUBCOMMITTEE ON HOUSING AND COMMUNITY OPPORTUNITY

of the

COMMITTEE ON FINANCIAL SERVICES

Regarding

"Simplifying the Home Buying Process: HUD's proposal to Reform RESPA"

February 25, 2003

Submitted by: Ira Rheingold
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Mr. Chairman and Members of the Committee, the National Association of Consumer Advocates[1] thanks you for inviting us to testify today about HUD's recent proposed rulemaking regarding the Real Estate Settlement and Procedures Act. We offer our testimony here today on behalf of our members and the tens of thousands of consumers they represent

Last July, the U.S. Department of Housing and Urban Development issued important proposed changes to RESPA regulations that attempt to dramatically alter the way the mortgage lending market operates. Initially, I'd like to commend HUD for taking bold action to reform the current RESPA regime that undeniably provides little benefit for consumers. HUD has recognized that changes must be made, and that it is the agency's responsibility to develop the necessary rules and regulations that will allow this important statute to achieve its purpose of protecting consumers in the mortgage settlement process.

The stated goals and orientation of HUD's Proposed Rule are exactly on target – to protect consumers. We believe that the proposal offers some very positive features that if properly implemented would improve the prime mortgage marketplace for consumers. These positive features include:

1. ***Requiring an Interest Rate and Closing Cost Guarantee when a Guaranteed Mortgage Package Agreement is offered.***

   Some parts of the mortgage industry are strongly pushing HUD to transform the GMPA into a package of closing costs instead of a package of all closing costs and points and interest rate. In its proposal, HUD has correctly refused to allow a section 8 exemption for a lender's offer of merely a closing cost package. After all, as HUD has recognized, a lender who offers a guarantee for the closing cost package, without also guaranteeing the points and the rate, has no impediment to simply increasing the points or the rate after the consumer is locked into using the lender because the closing cost package has been purchased.

2. ***HUD's attempt to recharacterize yield spread premiums as a payment from the lender to the borrower.***

   During the last several years, no issue has been more contentious than the use of yield spread premiums in the home mortgage lending process. Time and again, consumers have unknowingly received a mortgage with a higher interest rate than they had otherwise qualified for because of inappropriate and illegal

[1] The National Association of Consumer Advocates is The National Association of Consumer Advocates is a non-profit organization designed to promote justice for all consumers by maintaining a forum for information sharing among consumer advocates across the country. Our mission is to serve as a voice for consumers in the ongoing struggle to curb unfair and abusive business practices, especially in the areas of finance and credit.

kickbacks paid by lenders to brokers in the form of yield spread premiums. HUD's proposal to change the way yield spreads are disclosed is an important first step (although much more is needed) in allowing consumers to have greater control in choosing the type and structure of their loans and in the method choose to compensate *their* mortgage broker.

3. ***HUD's bright line rules that attempt to make the Good Faith Estimate a meaningful binding document that provides real information to consumers.***

Far too often, the Good Faith Estimate offered to consumers barely resembles the loan the borrower ultimately receives. HUD's proposed rule attempts to severely limit the bait and switch gaming rampant in the home mortgage marketplace involving closing costs. The GFE should be a true reflection of actually anticipated costs, not an opportunity for lenders to mislead consumers – as it is currently. Lenders who make numerous loans absolutely have the capacity to determine their own charges and those of settlement service providers that they choose and require.

While we strongly appreciate HUD's positive efforts, we nonetheless have several overarching concerns about the proposed rule and believe a myriad of important details must be worked through to ensure that the Rule does in fact protect consumers, instead of simply providing a shield behind which mortgage originators can hide inappropriate, unfair, and illegal activities. We will use the remainder of our testimony to broadly describe these problems.

Problems with HUD's Proposed Rule

1. ***These rules do not address predatory lending.***

As the Secretary has already noted in his testimony to the House Financial Services Committee on October 3, 2002, these rules do not provide the answer to predatory lending. It is imperative that HUD clarify that this Rule is not designed to address the problem of predatory lending and that other reforms are still needed. Indeed, HUD does not have the authority under RESPA to address predatory lending by itself in a global way. The rule is intended to facilitate shopping for mortgages and to promote competition. This laudable goal should be pursued. However, as victims of predatory mortgages are targeted by lenders who actively work to eliminate shopping opportunities, no amount of improvement to the RESPA rules will protect them.

2. ***These rules must avoid facilitating predatory lending.***

The Guaranteed Mortgage Package Agreement is a creative and novel proposal that, if implemented properly, will enable mortgage shoppers in certain markets to shop more effectively. However, we must keep in mind that shopping does not actually occur among all consumers – particularly those who are today the victims of predatory mortgages and those who will be targeted in the future. The predatory lending market thrives in an atmosphere in which lenders and brokers target homeowners and experience little pressure to provide the best products. Indeed, the incentives run in the other direction – borrowers are steered to the worst products. The GMPA must not provide a new means for lenders in the subprime market to avoid liability for non-compliance with consumer protection law in that segment of the marketplace that most needs more substantive consumer protection.

Because the GMPA ~~proposal~~ eliminates disclosures that otherwise make it possible for consumers and their advocates to evaluate compliance with both the Truth in Lending Act and the Home Ownership Protection Act, HUD must tread carefully in developing this RESPA rule and follow two essential principles:

- Limit the GMPA to the prime market - As the purpose of the GMPA is to encourage shopping in the open marketplace of competitive mortgage lending, the GMPA should only be provided to that section of the market that is most capable of using competitive pressures in the open marketplace to protect themselves – to the prime market.

- The GMPA rule should only be finalized after full coordination with the Federal Reserve Board – It is crucial that both regulators and consumers be able to determine compliance with TILA and HOEPA simply by looking at the information provided on the documents required by federal law. Under the current proposal, it is unclear that this will be the case and HUD must work with FRB to develop a transparent GMPA that allows for this determination to be made.

3. ***The substantive change proposed regarding yield spread premiums must be included in the regulations relating to RESPA's Section 8, not just as disclosures.***

For yield spread premiums to be what the mortgage industry claims them to be, merely one of several methods consumers can choose to compensate their mortgage brokers (and not an illegal kickback), enforceable regulations must be created that require the following:

- The consumer must be informed up-front just how much the mortgage broker will charge.

- The consumer must be provided the opportunity to choose how this payment will be paid from choices actually available to the consumer.

4. ***The Good Faith Estimate proposal rules, while good in concept, do not sufficiently protect consumers.***

This is particularly true of HUD's language describing the mortgage broker's relationship to the consumer. Section I of the proposed GFE allows brokers to describe themselves like this: "We do not offer loans from all funding sources and we cannot guarantee the lowest price or the best terms available in the market. You should compare the prices in the boxes below and shop for the loan originator, mortgage product, and settlement services that best meet your financing needs." Both of these statements must be deleted from the GFE.

In many states, a broker can establish an agency relationship with a borrower through the broker's conduct or by written and oral representations.[2] The broker may have fiduciary duties of an agent to the borrower, which may include the duty to advise the borrower of disadvantageous loan terms in an offered loan or the duty of loyalty to the borrower that would require the broker to seek out a loan with favorable terms for the borrower. HUD's statement in the GFE therefore conflicts with obligations that may be imposed on brokers under state law. Moreover, this misguided statement will undoubtedly be used, by unscrupulous brokers, to defeat borrower claims that a fiduciary relationship was established or that the broker made misrepresentations about the loan terms or the broker's role.

5. ***There must be effective enforcement mechanisms for an originator's failure to comply with all aspects of these new rules.***

Even perfect consumer protection rules will only work in the marketplace if they are enforced in a meaningful way. Lenders must have incentives to comply with the rules, because lack of compliance is too costly. The Proposed Rule does not currently include *any* mechanisms to punish transgressors. The proposal only provides that once the transgression is caught, the remedy is for the lender to provide what was promised all along. This rewards *lack of compliance* because the cost of being caught breaking the rules is the same as compliance. For the rules to be effective, HUD must allow for civil enforcement of each element under the rule including the requirements for treatment and disclosure of the yield spread premium, the new rules for the Good Faith Estimate, as well as for a lender's failure to keep the promises in the GMPA. This can be accomplished by:

- Removing HUD's stated prohibition against enforcing violations of section 8 through class actions. The 2001 Statement of Policy explicitly requires a court's individual review of each transaction, eliminating the efficient enforcement mechanism of class actions. Once HUD's Proposed Rules provide the new rules of the road, there is no reason a court cannot

[2] In addition, some states have passed legislation specifically regulating mortgage brokers and these laws may impose additional disclosure or substantive requirements.

evaluate and enforce the yield spread requirements in class reviews – as the only issue will be whether the mortgage broker actually gave the consumer the full benefit of the payment from the lender.

- A Statement from HUD articulating its belief that the failure to comply with proposed GFE rules is unfair and deceptive. This should enable some private enforcement under state and federal prohibitions against unfair and deceptive acts and practices.

- Creating a presumption establishing a lender's failure to follow the rules when offering a GMPA, or its failure to close on a loan that conforms to the GMPA violates RESPA's Section 8.

In summary, while we applaud HUD's positive efforts to reform RESPA, important detailed changes to their rulemaking must be implemented before HUD's stated goal of simplifying the mortgage market for the benefit of consumers can be achieved.

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Written Statement

of

Arne Rovick
Vice Chairman and General Counsel
Edina Realty Home Services

On Behalf of

The Real Estate Services Providers Council, Inc. (RESPRO®)

Before the
U.S. House of Representatives
Subcommittee on Housing and Community Opportunity
of the
Committee on Financial Services

On

"Simplifying the Home Buying Process:
HUD's Proposal to Reform RESPA"

February 25, 2003

Good afternoon, Mr. Chairman and members of the Subcommittee. My name is Arne Rovick and I am Vice Chairman and General Counsel of Edina Realty Home Services, a full service real estate brokerage company headquartered in Edina, Minnesota.

Edina Realty Home Services is the parent company of Edina Realty, Inc., which participated in over 33,000 residential real estate sales transactions in the year 2002 for a total volume of $7 billion, through 70 residential real estate brokerage offices and 2900 real estate sales associates in Minnesota and western Wisconsin.

Edina also is the co-owner along with Wells Fargo Home Mortgage of a joint venture called Edina Realty Mortgage, LLC, which originated over 6300 residential mortgages in the year 2002 for approximately $1 billion, and the parent of Edina Realty Title, Inc., which issued over 10,000 title insurance policies and performed 20,000 closings in the year 2002.

Today, I represent the Real Estate Services Providers Council, Inc. (RESPRO®), of which I was past Chairman and currently serve as a member of the Board of Directors.

RESPRO® is a national non-profit trade association of approximately 220 leading companies in the home buying and financing industry (see attached membership list). Our members represent a cross section of the industry, including real estate brokerage companies, mortgage lenders/brokers, title insurers/agencies, vendor management companies, and other settlement service providers.

RESPRO® members united in 1992 to promote an environment that allows providers from all industries to offer home buyers and owners the benefits of diversified services, known as "one-stop shopping."

Because RESPA's referral fee provision (Section 8) regulates the flow of funds to gain access to the consumer, any attempts to change it by either Congress or the

Department of Housing and Urban Development (HUD) inevitably create "turf battles" among industries that compete for that access.

RESPRO®, however, believes that our cross-industry membership gives us a broader perspective on RESPA issues than that of a single-industry association. RESPRO® members began to review "packaging" proposals similar to that proposed by HUD in its pending RESPA rulemaking as early as 1996. Despite our members' different industry perspectives and interests, we were able to agree on a "consensus" position on a packaging that is based upon the fundamental premise that consumers are better served if *all* providers, regardless of their industry or affiliation, can offer their products and services in an open and competitive marketplace. It is that premise that forms the basis of my testimony today.

I. Overview

RESPRO® supports HUD's goals of providing consumers (1) settlement cost information early in the process, (2) the ability to shop for the mortgage product and settlement services that best meet their needs, and firm disclosed costs that would avoid surprises at settlement; (3) the benefit of new products, competition and technological innovations that could lower settlement costs; (4) access to better borrower education and simplified disclosure; and (5) vigorous RESPA enforcement and a level playing field for all industry providers. [1]

However, RESPRO® believes that HUD's specific proposal to give lenders a RESPA safe harbor for guaranteeing an entire loan "package" at the time of application would not accomplish these goals because (1) virtually all lenders and certainly all non-lenders are unable to guarantee the interest rate as HUD's proposal would require them to do; (2) non-lenders such as real estate brokers, home builders and title or other settlement

[1] "Martinez announces 'Homebuyer Bill of Rights'— Part of Bush Administration Effort to Expand Homeownership", HUD Press Release (June 26, 2002).

service companies would as a practical matter be excluded from competing in the packaging marketplace; and (3) consumers could not effectively shop among packages because the services included in the package would not be required to be itemized and consumers would have no way of comparing the contents of each package.

To correct these deficiencies, RESPRO® has proposed to HUD a "Two-Package Concept" that would (1) make it more viable for lenders and non-lenders to package by eliminating the guarantee of the interest rate; (2) increasing competition in the packaging marketplace by allowing non-lenders like real estate brokers, home builders, and title or settlement service companies to offer settlement service packages directly to consumers; (3) allowing consumers to compare packages by itemizing the services in each package; and (4) preventing unscrupulous lenders from engaging in "bait and switch" techniques that involve increasing an interest rate at the last minute to make up for price concessions on a settlement service package.

RESPRO® also believes that HUD's proposed "binding Good Faith Estimate (GFE)" – the only alternative to "packaging" -- would significantly disrupt the marketplace by increasing liability risks for lenders, creating consumer confusion, and increasing administrative burdens for providers in all industries. Therefore, RESPRO® recommends that HUD leave the current regulatory environment in place as the packaging option is being tested in the marketplace.

II. <u>The Guaranteed Mortgage "Package"</u>

HUD's proposed rule would attempt to encourage mortgage lenders to offer a "Guaranteed Mortgage Package" three days after application, which would include a guaranteed interest rate subject to changes in a verifiable market index yet to be established and a total lump-sum cost for all settlement services the lender requires to close the loan (e.g., underwriting fee, appraisal, credit report, pest inspection, title insurance, closing services). The guarantee would be good for 30 days or until the consumer accepts the package.

Lenders who offer a "Guaranteed Mortgage Package" would be provided a safe harbor under RESPA's anti-kickback prohibition (Section 8) for transactions involving services within a loan "package". This would allow them to negotiate volume discounts with providers of services to be included in the package, be paid by third party providers for including their settlement services within the package, require the use of affiliated settlement services, and offer affiliated settlement services without providing the RESPA-required affiliated business disclosure.

While RESPRO® supports HUD's goal of promoting consumer shopping, we do not believe that its proposed Guaranteed Mortgage Package (which we will refer to as "HUD's packaging proposal") would achieve this goal for several reasons.

A. The Interest Rate Guarantee Would Not Be Viable for Lenders

Under HUD's packaging proposal, lenders would only get a RESPA safe harbor if they offer a guaranteed interest rate for 30 days to virtually anyone who inquires about a loan, provides basic income information about himself, and estimates the property's value. They would be expected to guarantee the rate with the knowledge that a large majority of potential borrowers would not in fact close their loans with them, although they could if interest rates rise above the guaranteed rate.

While HUD proposes to allow the interest rate to vary according to a verifiable index or other appropriate measure (which to date no one has been able to establish), lenders set prices according to the present cost of funds, which change hourly, if not more frequently, according to a long list of market factors and perceptions about such factors.

Given this environment, it is no sooner possible to guarantee an interest rate against an index than it is to guarantee a stock's movement or a stock or interest rate option against an index. While interest rates, stocks, and options may sometimes move consistent with the prime rate, the federal funds index, the Dow Jones, or Wilshire 5000, the rate of any one loan product can change numerous times before an index even blips and may change more or less than the rates of other similar loan products. Lenders would not be able to hedge that kind of risk in a volatile secondary market.

B. HUD Would Severely Limit Competition in the Marketplace by Not Allowing Non-Lenders (Real Estate Brokers, Home Builders, and Title/Settlement Service Providers) To Offer Guaranteed Packages

Even if it was possible to for lenders to guarantee the interest rate, HUD's "Single Package" approach as a practical matter would bar non-lenders such as real estate brokers, home builders, title underwriters and agents, vendor management companies and other settlement service providers from competing with lenders in the packaging marketplace because they do not offer and therefore could not guarantee the interest rate or the loan origination services that HUD requires to be included in the package. Instead, they would be forced to partner with a lender if they want to offer a guaranteed settlement service package.

As a result, competition that is supposed to pass on cost savings to consumers will be diminished, not promoted.

Let me give you an example, from the perspective of Edina Realty Home Services. Thirty percent (30%) of Edina's real estate customers choose Edina Realty Mortgage as their mortgage lender, but seventy percent (70%) choose their mortgage loan from over 100 other national, regional, or local mortgage lenders or brokers in any given year. Our title company, Edina Realty Title, Inc., currently issues title policies and performs closings on behalf of Edina Realty Mortgage *and* these 100 other mortgage lenders or brokers for seventy percent (70%) of Edina's real estate customers.

Edina Realty Title would like to offer guaranteed settlement service packages directly to our real estate customers that could be used not only with mortgages provided by Edina Realty Mortgage, but by any of the more than 100 mortgage originators in our marketplace. RESPA's referral fee prohibition would prevent Edina Realty Title from paying our real estate agents for referrals to our package, and it would mandate that we would disclose the affiliation to the consumer.

HUD's proposal, however, would prevent Edina Realty Title from offering these packages because it could not guarantee the interest rate and points, even though it could offer superior service and pricing with respect to all the services needed to close the transaction. Not only would this allow Edina to offer our real estate customers the potential benefits of packaging, but it would also provide small, local mortgage originators in our marketplace a means to compete against the large national lenders who package.

Edina is not alone in our willingness to compete in the new packaging marketplace. According to a 1997 study by Weston Edwards and Associates, 31% of the nation's 250 largest residential real estate brokerage firms offered title, closing, escrow or personal insurance in 1996 through wholly-owned subsidiaries or joint ventures. RESPRO® believes that this percentage has significantly increased over the last six years. In addition, a significant and increasing number of home builders offer these services.

The exclusion of these and other non-lender competitors (such as independent title companies) from the packaging marketplace would effectively put control over the distribution and marketing of settlement service packages in the hands of mortgage lenders. This would give lenders the ability to use the RESPA safe harbor to obtain lower prices and/or referral fees from non-lenders who provide settlement services to be included in the package without any assurance that competition in the packaging marketplace would be sufficient to ensure that any discount or lower price is passed on to the consumer.

In addition, the exclusion of non-lender competitors from the packaging marketplace could deprive consumers of potential benefits of one-stop shopping programs.

In fact, a 2002 survey of over 2000 current and future home buyers by Harris Interactive, the parent of Harris Poll, found[2]:

- That 82% of home buyers would "strongly" or "somewhat" strongly consider using a realty-based one stop shopping service for their home purchase;
- That 64% of home buyers who recently used realty-based one stop shopping programs had a much better overall experience with their home purchase transaction; and
- That over 90% of home buyers who did not use realty-based one stop shopping programs believed that if they had used one, they would have had a better overall home purchase experience.

A 1994 economic study commissioned by RESPRO® and conducted by Lexecon, Inc., a national economic consulting firm, also found that realty-based one stop shopping programs potentially offer lower costs. The study compared title and closing costs between realty-owned title companies and independent title companies in over 1000 home purchase transactions throughout seven states -- Florida, Minnesota, Tennessee, Wisconsin, Mississippi, Pennsylvania and California—and concluded that title and closing costs for realty-owned title companies were not only competitive with those of independent title companies, but actually resulted in a 2% cost savings.[3]

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2 "Consumer Perspectives on Realty-Based One Stop Shopping", by Harris Interactive and Murray Consulting, Inc., March 2002.

3 "Economic Analysis of Restrictions on Diversified Real Estate Services Providers", by Lexecon, Inc., January 3, 1995. In a 1996 Economic Analysis accompanying a final RESPA regulation, the Department of Housing and Urban Development (HUD) offered its independent analysis of both the Lexecon, Inc. study and the Edwards study. It concluded that "...referral activity among affiliates might still benefit consumers because

C. Consumers Would Not Be Able to Effectively Shop Among Packages Because Services in the Package Are Not Itemized

Many proponents of packaging believe that consumers do not care about specific settlement services associated with a mortgage loan; instead, they believe consumers only care about price. RESPRO® disagrees with this premise, especially in purchase money transactions.

HUD's packaging proposal partially recognizes that this premise is flawed, and therefore suggests in its packaging proposal that consumers at least be informed about whether particular services -- pest inspections, lenders title insurance, and appraisals -- are expected to be excluded from the package.

However, RESPRO® does not believe HUD's packaging proposal goes far enough to promote consumer shopping, and believes that all services included in the package should be disclosed to the consumer.

Consumers often are directly affected by the type of settlement services provided by the lender (e.g., automated valuation from statistical models, drive by, or appraisal based on an in-home inspection, pest inspection). In particular, in purchase money transactions, consumers often take solace that the lender has had a full appraisal or has performed a full title search, rather than simply assuming the statistical risk that its overall losses from loans will be acceptable.

Likewise, in certain geographic areas, special settlement services may be of great interest to consumers. For example, in some areas a consumer may want to know that lenders have specifically had the house inspected for mold, radon or stucco problems and if such inspections were not done he/she may want to pay for them directly or go with another packager who utilizes them.

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of the possibility of immediate savings in shopping time and hassle and future reductions in prices due to lower marketing and other costs. Taking these benefits into account, referrals among affiliated firms are probably neutral and possibly beneficial to consumers."

In addition, if services included in the package are disclosed, non-lenders such as real estate brokers and home builders – who in purchase money transactions work closely with the consumer and are the likely point of contact when future problems arise due to the omission of a settlement service – would be able to compete in the packaging marketplace on service as well as price.

D. RESPRO®'s Proposed "Two Package" Concept

Despite our concerns, we believe that HUD's goals of promoting consumer shopping may still be achieved if it restructures its packaging proposal.

As we understand it, HUD's proposal to include the interest rate in its proposed Guaranteed Mortgage Package is based upon a concern that a lender could engage in a "bait and switch" technique by offering a low-cost settlement service package and then making up for the price concession through a higher interest rate loan.

But we believe that HUD could significantly deter the use of "bait and switch" techniques – and at the same time inject competition into the packaging marketplace by ensuring that consumers can choose among guaranteed settlement service packages offered by *both* lenders and non-lenders -- by providing a RESPA safe harbor for transactions involving settlement services in two separate packages:

- **A "Lender Services" Package:** A package of itemized lender services required for the loan [the "800" series of the HUD-1 Settlement Statement), excluding the interest rate, that lenders could offer at a lump sum guaranteed price; and

- **An "Ancillary Services" Package:** A package of itemized non-lender services required for the loan (the "1100, 1200, and 1300" series of the HUD-1 Settlement Statement) that lenders *or* non-lenders could offer at a lump sum guaranteed price.[4]

Under RESPRO®'s proposed Two-Package Concept, a home buyer could choose among national, regional, or local mortgage originators for a "Lenders Services" package. At the same time, he/she could choose among a variety of "Ancillary Services" packages offered either directly or online by the mortgage lender or broker whose loan they choose, an affiliated title company of the real estate broker or home builder that is working with them on the purchase of their home, or an independent title company or other "packager".

This would help ensure that consumers could effectively shop for the lowest package of settlement services from a broad array of competitors.

RESPRO® recognizes that a mortgage lender should not have to accept an Ancillary Service package that utilize settlement service providers with a record of poor service or reliability, who cannot financially stand behind their products, or who have other documentable deficiencies. In other words, a lender should be able to reject an Ancillary Service package for legitimate business reasons.

In fact, we would anticipate that most Ancillary Service packages would be pre-approved by lenders and marketed by Ancillary Service packagers as acceptable by designated lenders.

However, it is also important to prevent lenders from raising the interest rate of a loan to offset price concessions given on a low-cost Ancillary Services package that it may offer. Therefore, RESPRO® proposes that lenders be prohibited from "tying" their loan or Lenders Services Package to the use of a particular Ancillary Service package; similarly, the Ancillary Service packager

[4] Under RESPRO®'s proposal, referrals between a real estate broker, homebuilder, or non-settlement service packager and the Ancillary Services package would still be subject to RESPA, so that they could not accept payments for referrals to the package, they must disclose the nature of the affiliation to the consumer, and they could not require the use of an affiliated package.

should not be permitted to tie or condition the use of its package on the use of a specific loan or interest rate.

In summary, RESPRO® believes that its proposed Two Package Concept would address HUD's concern that prompted it to require a virtually impossible guarantee of interest rates, which would threaten the viability of packaging. It also would inject greater competition into the packaging market for ancillary services to the loan than HUD's packaging proposal.

IV. The Binding Good Faith Estimate (GFE)

A. HUD Should Allow Packaging a Chance to Be Tested Without Marketplace Disruption By Leaving the Current Regulatory Environment as the Alternative to Packaging

RESPRO® opposes HUD's proposal to make the Good Faith Estimate (GFE) binding at this time, and recommends that HUD leave the current regulatory environment as the alternative to "packaging".

1. Packaging Should Be Tested in the Marketplace Before the Alternative Regulatory Environment is Significantly Altered

In the opening statement of its proposed RESPA rule, HUD says, "The American mortgage finance system is justifiably the envy of the world. It has offered unparalleled financing opportunities under virtually all economic conditions to a very wide range of borrowers that, in no small part, have led to the highest homeownership rate in the Nation's history. "

HUD clearly recognizes in this statement that our residential mortgage industry has functioned well. In addition, the residential real estate industry has been one of the strongest sectors of our nation's economy for the past three years.

This is not to say, however, that the mortgage process cannot be improved. We welcome the opportunity to test the economic theories supporting RESPRO®'s Two Package approach. However, we believe that HUD should be cautious about dramatically changing the pricing and delivery system for such a crucial sector of our economy until it has tested the theories of the packaging system and can predict with certainty that the GFE proposal is viable.

2. HUD's Proposed Binding GFE Would Significantly Increase Liability Risks for Mortgage Lenders

HUD's proposed binding GFE would dramatically increase liability risks for lenders who do not package by requiring them to control costs that are outside of their ability to control, without the incentives HUD provides for packagers.

Mortgage lenders do not have control over and often cannot estimate within a "ten percent" or "zero" tolerance the charges of many third party services, such as state and local government charges, which are totally in the control of the government; reserves for the cost of hazard insurance, mortgage insurance, and/or property taxes, each of which are very difficult to predict and may in part depend on when a closing will be held; title charges, which are dependent on many factors not known at the time of application (e.g., in some states the preliminary title report is based upon abstract entries which depend on what the seller has done which means you need an examination of the property, likewise, certain inspections may be triggered by an appraisal).

These significant liability risks are compounded by HUD's proposed remedy for non-compliance with its binding GFE requirements – a rescission of the loan agreement, or, in HUD's words, allowing the borrower to withdraw the application and receive a full refund of all loan related fees and charges if the cost at settlement exceeds the estimate and permissible tolerances on the GFE (absent "unforeseeable and extraordinary" circumstances).

Rescission of the loan is an extreme and excessive penalty, especially if the violation is technical and/or unintentional. For example, under HUD's proposal, a lender in a refinancing transaction whose closing costs in a particular category exceed the GFE estimate by a minor amount would be vulnerable to a borrower's decision to walk away from the transaction at the last minute and collect all loan-related fees paid if he/she finds a better interest rate, with no opportunity to correct the mistake and refund the difference between the GFE estimate and the actual closing cost.

HUD's rescission penalty also is unclear as to when the consumer could withdraw the application and receive the refund of all loan related fees and charges. Presumably, this could occur at closing; although it is doubtful that a buyer of a home will choose to withdraw his/her loan application in a purchase money transaction and possibly forfeit the home of his/her dreams. If HUD allows a rescission and refund of all loan-related fees after closing, it would create considerable confusion in the secondary mortgage market.

3. <u>HUD's Proposed Binding GFE Is Confusing to the Consumer</u>

HUD's proposed binding GFE is seven pages long. While the estimated charges are presented on the first page, the proposed form uses terms that are not familiar to the average consumer (e.g., "lender-required and selected third party services", "shoppable lender required third party services") that require several pages of attachments to explain. In addition, the tolerances for each category of charge are explained in several pages of attachments. Finally, since both HUD's packaging and GFE proposals presume incorrectly that consumers only care about price and not service or convenience, and because the GFE has no description of the particular service and what's included in it, it would be extremely difficult for a consumer to make "apples to apples" comparisons of packages offered by different settlement service providers.

4. HUD's Proposed Binding GFE Would Create Significant Administrative Burdens on Providers Across Industry Lines That Are Not Anticipated in Its Economic Analysis

RESPRO® believes that this resulting consumer confusion over the terms, format, and tolerances in new binding GFE would generate consumer questions that will necessitate extensive consultations with providers, resulting in considerable education and training costs to providers across industry lines.

For example, most home buyers would consult with their real estate agent to help guide them through the new terms, format, and tolerances in the new binding GFE, as they do today with their questions about the GFE. We believe that HUD has severely underestimated the significant education and training costs that would be incurred by the real estate brokerage industry in purchase money transactions if the binding GFE were implemented.

Moreover, mortgage originators and loan closers have invested in software that helps prepare GFE's and HUD-1's, and that material changes to either form will cause further substantial expense to both of these industries.

Finally, between the application and the closing, there are usually loan term changes in the loan, the loan amount, and even property type that often trigger additional services and costs that could not be foreseen at the time the binding GFE is provided. As a result, mortgage lenders in a significant number of loan transactions would need to reissue the binding GFE every time there is a change in the loan terms, resulting in more consumer confusion and significant administrative costs for providers across industry lines.

5. HUD Does Not Have The Statutory Authority To Implement The Proposed GFE With Tolerances And Rescission Rights For Borrowers Through Regulation

RESPA requires that a mortgage lender, within three days of receipt of a loan application, provide the applicant with a "good faith estimate of the amount of charges for specific settlement services the borrower is likely to incur in connection with the settlement as prescribed by the Secretary." There is no private remedy or private right of action for a lender's failure to comply with this requirement.

Indeed, Congress had once provided in RESPA for an advanced and itemized disclosure of charges arising in connection with the settlement, as well as for lender liability for failure to comply. Congress later repealed this part of RESPA, deciding not to impose any sanctions for violation of the new good faith estimate provision even though other parts of RESPA did provide for private remedies and rights of action.

HUD's proposed regulation rewrites RESPA. It converts an estimate of settlement charges with no penalties into a provision where lenders would have to itemize with complete accuracy certain charges in advance and predict others within a ten percent tolerance subject to the right of a borrower to withdraw, or in effect rescind, their loan application if the lender's estimate was faulty. We do not believe that HUD does not have this authority.

Mr. Chairman, RESPRO® appreciates this opportunity to testify, and I would be glad to answer any questions.

Effective 2/19/2003

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Houston, TX
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Relaty World, John Horton & Associates
Austin, TX

Testimony before the

FINANCIAL SERVICES COMMITTEE

Subcommittee on Housing and Community Opportunity

regarding

Simplifying the Home Buying Process: HUD's Proposal to Reform RESPA

February 25, 2003

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Mr. Chairman and Members of the Committee, the **National Consumer Law Center**[1] thanks you for inviting us to testify today regarding the HUD's proposal to rewrite the RESPA. We offer our testimony here today on behalf of our low income clients, as well as the **Consumer Federation of America, Consumers Union,** and the **U.S. Public Interest Research Group.**[2] The **U.S. Public Interest Research Group** is the national lobbying office for state PIRGs, which are non-profit, non-partisan consumer advocacy groups with half a million citizen members around the country.

We wish to commend Secretary Martinez for the dramatic approach to RESPA[3] reform advocated in these Proposed rules. Clearly, the Department has recognized that the current state of RESPA's consumer protection is a murky mess. For example, to the extent that RESPA's current regulations provide rules that protect consumers, these rules are generally unenforced or are unenforceable by the courts. Some changes must be made, and it is HUD's responsibility to articulate the means by which this important statute will effectuate its purpose of protecting consumers in the mortgage settlement process.

The stated goals and orientation of the Proposed Rule are wonderful – to protect consumers. We credit the hard work and creativity of HUD staff in the conception of this Rule. We applaud the many positive features of these proposals, and hope that HUD has accepted the comprehensive comments[4] we

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[1]The **National Consumer Law Center** is a nonprofit organization specializing in consumer issues on behalf of low-income people. We work with thousands of legal services, government and private attorneys, as well as community groups and organizations, from all states who represent low-income and elderly individuals on consumer issues. As a result of our daily contact with these advocates, we have seen examples of predatory practices against low-income people in almost every state in the union. It is from this vantage point – many years of dealing with the abusive transactions thrust upon the less sophisticated and less powerful in our communities – that we supply these comments. We have led the effort to ensure that electronic transactions subject to both federal and state laws provide an appropriate level of consumer protections. We publish and annually supplement twelve practice treatises which describe the law currently applicable to all types of consumer transactions.

[2]The **Consumer Federation of America** is a nonprofit association of over 280 pro-consumer groups, with a combined membership of 50 million people. CFA was founded in 1968 to advance consumers' interests through advocacy and education.

Consumers Union is the publisher of Consumer Reports.

[3]The Real Estate Settlement and Procedures Act ("RESPA"), 12 U.S.C. § 2601, *et seq.*

[4]As this testimony can only provide a summary of the many issues which must be addressed in the proposed rules, we point you to the comprehensive comments that we filed with HUD, available on our website at www.consumerlaw.org. Our comments to HUD were provided on behalf of our low income clients, five national consumer advocacy groups, as well as the clients of 17 legal services programs in urban and rural areas throughout the nation. *See*, Appendix 1.

submitted in the spirit in which they were offered – as constructive so as to assist HUD in achieving its goals of creating a regulatory regime under RESPA that is truly protective of consumers – which is the purpose of RESPA.

There are several overarching concerns and a myriad of important details which must be worked through to ensure that the Rule does in fact protect consumers, instead of simply providing a shield behind which mortgage originators can hide inappropriate, unfair, and illegal activities. While the overall concepts are good, there are significant changes in the details of the rules which must be made to prevent substantial harm to consumers. However, we want to be absolutely clear that our most important concern has to do with the Rule's potential to *facilitate* predatory lending.

> **The single most critical point for the representatives of low and middle income consumers providing these comments is that HUD limit the Guaranteed Mortgage Package Agreement ("GMPA") to prime loans. If subprime loans are permitted to be made through the GMPA structure, *predatory lending* will be facilitated and protected by the GMPA exemption.** This means that HUD must go *beyond* its current proposal to exclude only HOEPA loans from the GMPA exemption, and exclude all loans with subprime characteristics.

Major Concerns

I. To avoid facilitating predatory lending, the GMPA should be limited to prime loans.

The idea behind the Guaranteed Mortgage Package Agreement ("GMPA") is to simplify the mortgage shopping process by both bundling the loan closing costs with the loan points, and providing an interest rate guarantee based on the borrower's credit qualifications. This would accomplish two important goals: 1) It would allow borrowers to shop for loans based simply on the interest rate and the money required to obtain the loan; and 2) It would permit borrowers to apply to numerous lenders and receive guarantees of the loans for which they actually qualify, subject only to verification of the information the consumer has provided about the value of the home, the borrower's income, and other assets. The most important aspect of the GMPA is that it allows borrowers to obtain loan guarantees based on their actual credit rating very early in the process. This will prevent tremendous misunderstanding and allow borrowers with less than perfect credit to participate fully in the shopping process.

Portions of these comments are reiterated in this written testimony.

The GMPA is a creative and novel proposal which, if implemented properly, will enable mortgage shoppers in *certain markets* to shop more effectively. However, HUD must keep in mind that this shopping does not occur among all consumers – those who are today already the victims of predatory mortgages and those who will be targeted in the future. This submarket thrives in an atmosphere in which lenders and brokers target homeowners and experience little pressure to provide the best products. Indeed, the incentives run in the other direction – borrowers are steered to the worst products. The GMPA must not provide a new means for lenders in the subprime market to avoid liability for non-compliance with consumer protection law in that segment of the marketplace which most needs *more* substantive consumer protection.[5]

As the GMPA streamlines disclosure of specific charges and services it will allow mortgage originators to hide illegal fees and insulate lenders from legal challenges under both RESPA and the Truth in Lending Act ("TILA").[6] It was HUD's intent to trade compliance with the specific requirements of RESPA's Section 8.[7] However, an *inadvertent* result of the GMPA will be to conceal information needed to determine the accuracy of TILA disclosures as well, providing legal insulation from both federal laws. One of the effects of the bundling of loan fees under the Guaranteed Mortgage Package ("GMPA") will be that TILA compliance will no longer be discernable by a comparison of the TILA disclosure and the HUD-1.[8] High cost loans may be successfully camouflaged from challenge under TILA regulations, or even HOEPA compliance, as a result. Neither bank regulators nor others reviewing mortgage loans will be able to perform accurate compliance reviews.

As the purpose of the GMPA is to encourage shopping in the open marketplace of competitive mortgage lending, the GMPA should only be provided to that section of the market which is most capable of using competitive pressures in the open marketplace to protect themselves – to the prime market. This is essential. **To ensure that HUD's new GMPA does *not* facilitate and protect predatory loans from**

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[5]We have supported the concept of the GMPA in the past in the context of statutory change in the law. Amending the RESPA and TILA statutes would allow all the overlapping issues of disclosures under both statutes, enforcement, and protections against predatory lending, to be addressed together. Attempting to address the disclosure problems of RESPA only through regulation unfortunately creates serious implications for enforcing TILA requirements and removes existing protections against predatory lending. *See* Margot Saunders, Testimony Regarding the *Rewrite of Truth in Lending Act and Real Estate Settlement Procedures Act* (Sept. 16, 1998), available on-line at http://www.consumerlaw.org/initiatives/predatory_mortgage/sen_mortg.shtml.

[6]15 U.S.C. § 1601 *et seq.* Currently, compliance with TILA's required allocation of fees between amount financed and finance charge can be tested only by comparing the disclosure of specific fees provided on the RESPA HUD 1 with the statements of the disclosures provided on the TILA form. Though TILA generally requires the lender to provide the borrower with an itemization of the amount financed unless the consumer opts out, lenders need not give this itemization if they provide both the GFE and the HUD-1. Official Staff Commentary § 226.18(c)-4.

[7] 12 U.S.C. § 2607.

[8]This situation may change if the Federal Reserve Board issues new regulations or new comments under TILA requiring otherwise. These comments evaluate the effect of the Proposed RESPA Rule on existing interpretations of TILA rules.

legal scrutiny, any loan that meets any one of the following triggers should *not* be permitted to be made as a GMPA –

- Any HOEPA loan
- Any loan with a prepayment penalty.
- Any loan with a guaranteed mortgage package price (the single fee) – which equals or exceeds 5% of the principal of the loan.

A. HOEPA loans can be mischaracterized, yet protected from challenge in a GMPA

The Home Ownership and Equity Protection Act, passed in 1994,[9] does not cure the problem of abusive home equity lending. The law continues to allow high rate home equity loans to be made and does not regulate excessive interest rates or fees per se. Its coverage is limited, excluding loans with high rates and fees just under the trigger amounts, open-end home equity credit, and reverse mortgages.[10] Extraordinarily abusive loans can continue to be made without triggering HOEPA protections because lenders can easily circumvent HOEPA by charging rates and fees just under the HOEPA trigger amounts.

As a result, in many high cost loans, there is litigation regarding whether the fees charged by the lender have been properly allocated to the HOEPA points and fees trigger. Many loans are treated by lenders as non-HOEPA loans, only to be determined later by regulators or attorneys for consumers to have been wrongly excluded from HOEPA. Once it is shown that a loan should have been covered by HOEPA, but was not, considerable consumer protections then apply.[11] A lender who violates the requirements of HOEPA faces enhanced statutory penalties as well as rescission of the loan.[12] The protections of HOEPA are thus most often helpful to consumers when they have been breached – because they provide substantial assistance in avoiding foreclosure on loans which included abusive terms.

The HUD-1 required by RESPA satisfies the requirement under TILA that an itemization of the amount financed be made available to the borrower. This itemization is critical for determining not just TIL compliance but also whether the loan is covered by HOEPA. The GMPA would make it impossible for consumers - or regulators - to determine whether a loan presented as a non-HOEPA loan was actually a HOEPA loan.

This is why the GMPA cannot be permitted to mask the fees of loans which are anywhere in the neighborhood of HOEPA loans – else substantially abusive loans will be made under the rubric of the GMPA, thus denying to consumers the ability to test these loans for compliance with the Truth in Lending Act and appropriate exclusion from HOEPA.

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[9]Codified at Section 129 (15 U.S.C. § 1639) and in Sections 31 and 32 of Regulation Z (12 C.F.R. § 226.31 and 226.32).

[10] 15 U.S.C. §1602(aa)(1).

[11]For example, only HOEPA loans require the extra disclosure required three days before closing, as well as limitations of the circumstances in which prepayment penalties can be charged (15 U.S.C. § 1639(c)), special requirements for payments made to home improvement contractors ((15 U.S.C. § 1639(i)), and prohibitions on extending credit without regard to the consumer's payment ability (15 U.S.C. § 1639(h)).

[12]15 U.S.C. § 1640(a) and 15 U.S.C. § 1635.

B. All subprime loans should be excluded from the GMPA.

We know the *characteristics* of *predatory* loans. HOEPA only covers a small percentage of subprime loans.[13] The HOEPA triggers suggested by HUD in the Proposed Rule do not provide nearly enough protection. Currently advocates estimate the bulk of predatory loans finance between 5 to 8% of the principal of the loan as points, fees and closing costs.[14] HUD has already stated that financing more

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[13] Federal Reserve Board, Final Rule, Statement of Basis and Purpose, 66 Fed. Reg. 65604, 65607 (Dec. 20, 2001).

[14] This information is gleaned from the hundreds of loan documents reviewed each year by the attorneys providing these comments. See also Washington Department of Financial Institutions, Expanded Report of Examination for Household Financial Corporation III as of April 30, 2002, at 48 (finding that Household charged 7.4% in upfront costs on most loans), *available from* the National Center on Poverty Law as Clearinghouse No. 54,580.

than 3% of points and fees is a sign of a predatory loan.[15] Further, in its regulations of the GSEs HUD has prohibited the provision of housing credits for loans in which more than 5% of the principal has been charged.[16] It is also important to note that many of the new anti-predatory lending laws passed by the states have used 5% points and fees as a trigger for coverage.[17]

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[15] *See*, Joint HUD-TREASURY Report on Recommendations to Curb Predatory Home Mortgage Lending, June 20, 2000, at page 11. http://www.hud.gov/library/bookshelf18/pressrel/pr00-142.html. The agencies noted the dangers to homeowners of financing high fees:

> Financing points and fees may disguise the true cost of credit to the borrower, especially for high interest rate loans. Restricting the financing of points and fees for HOEPA loans would cause these costs to be reflected in the interest rate, enabling borrowers to better understand the cost of the loan, and to shop for better terms.

[16] *See* 24 CFR 81.16(b)(12) and 24 CFR 81.2. These regulations do allow third party fees paid for closing costs to be excluded from the 5% calculation. However, as these fees would not be itemized on the GMPA, excluding some fees would not be possible. It is also far better, at this point of the development of this new product to exclude too many loans, rather than to include too many, and limit enforcement of existing law on predatory mortgages as a result.

[17] *See, e.g.* N.C.G.S. S.L. 1999-332; Ga. Code Section 7-6A-1 *et seq.*; 2001 N.Y. A.B. 11856 (SN) (Oct. 3, 2002).

Thus, to ensure that HUD's new GMPA does *not* facilitate and protect predatory loans from legal scrutiny, any loan that meets any one of the following triggers should *not* be permitted to be made as a GMPA: any HOEPA loan. any loan with a prepayment penalty, and any loan with a guaranteed mortgage package price (the single fee) – which equals or exceeds 5% of the principal of the loan.

In other words – in addition to HOEPA loans, any loan which has *either* a prepayment penalty, *or* the price for the GMPA is equal to or more than the 5% of the loan principal – must not be eligible for the exemption outlined in the Proposed Rule. Any lender making a loan with either of these criteria would still be required to itemize the fees paid to settlement service providers pursuant to the rules for the Good Faith Estimate.

1. GMPA should not be permitted for loans with high points and fees

As predatory loans generally charge high points and fees it is essential that the GMPA not be permitted to be provided for these loans. The most meaningful mark of a predatory loan is in the high amount of points and fees[18] financed by the borrower. The more the borrower is charged up-front, the more the immediate financial gain achieved by the lender. This is why many of these loans are not affordable to the homeowner – the lender has an incentive to make them non-performing loans. If that loan does not perform such that the homeowner is forced to refinance, it just means more profit for the lender at each refinancing. For the homeowner, it means more equity is stripped from the home each time.

Using 5% of the principal as the trigger for exclusion from GMPA eligibility will still allow loans with very high up-front cost to be made with a GMPA. According to various studies, closing costs on conventional mortgages rarely exceed 2% of the loan amount.[19] Using 5% as the trigger allows ample – perhaps too much? – room to ensure that all prime loans for which a GMPA might be appropriate would be eligible for the competitive benefits of the GMPA. However, this figure also ensures that loans which are not truly competitive are excluded from the exemption.[20]

2. GMPA should not be permitted for loans with prepayment penalties

Prepayment penalties also are the mark of a predatory loan, and lenders providing GMPAs should not be permitted to include prepayment penalties.

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[18] We include in our definition of fees the high costs of single premium credit insurance.

[19] According to the Federal Housing Finance Board's "*Monthly Interest Rate Survey,*" Table 1: Terms on Conventional Single-Family Mortgages, Annual National Averages, All Homes, *available at* www.fhfb.gov/MIRS/mirs_t1.xls, initial fees and charges average less than one point from 1995 through 2000 on conventional residential mortgages.

[20] For example, a loan of $150,000 would be permitted to have a GMPA package cost of $7,499. A $200,000 loan could have a GMPA price of $9,999. These up-front costs are actually much higher than most competitive, prime loans would ever charge for up-front closing costs. To the extent that the figure of 5% may represent too small a sum to compensate lenders for their up-front costs when making small loans (for example loans of less than $75,000), the 5% trigger could be adjusted upwards. However, just as this figure is adjusted upwards for smaller loans, the 5% trigger should also be adjusted lower for loans of larger amounts.

When a lender extends considerable expenses in the making of a loan, the lender does risk loss if the loan is prepaid before the regular payments on the loan allow the recoupment of these expenses. In the prime mortgage market, the effect of competition protects lenders: the low interest rate the borrower currently has discourages the borrower from prepaying the loan. Typical prime mortgage loans stay on the books for an average of five years. Thus only 2% of prime loans have a prepayment penalty.[21]

However, fully 70% of subprime loans have prepayment penalties because of lack of perceived options on the part of the borrowers.[22] In the subprime mortgage market, the brokers are generally the gatekeepers for the loans, and they operate on the reverse competition method of yield spread premiums. The higher the premium paid to a broker, the more likely the broker will match a lender up with an unwitting borrower. The hefty price paid to the broker in the yield spread premium is an expense that the lender must recoup in order to avoid a loss, especially considering that the same broker has an incentive to market aggressively another loan to the same borrower. Thus, the lender must charge prepayment penalties to protect itself from the costs incurred by yield spread premiums.

If prepayment penalties were disallowed, unreasonable yield spread premiums would not be paid by lenders, because they could not afford the risk. This would not mean that loans would not be made – they are made every day in the prime market without hefty premiums and prepayment penalties. As yield spread premiums are completely masked in the GMPA – unreasonable yield spread premiums should not be encouraged by allowing loans with prepayment penalties to be included in the exemptions offered by the GMPA.[23]

It is clear to many that prepayment penalties on subprime loans have virtually nothing to do with lowered interest rates.[24] It therefore cannot be argued that precluding loans with prepayment penalties

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[21]See Freddie Mac, Frequently Asked Questions on Prepayment Penalties, *available at* http://www.freddiemac.com/singlefamily/ppmqanda.html

[22]*See* Gail McDermott, Leslie Albergo, Natalie Abrams, Esq., NIMS Analysis: Valuing Prepayment Penalty Fee Income Standard & Poor's, News Release, Jan. 4, 2001. *Also see,* North Carolina Coalition for Responsible Lending, Prevalence of Prepayment Penalties, available at http://www.responsiblelending.org/PL%20-%20Coalition%20Studies.htm citing data obtained in an interview with the Mortgage Information Corporation and the industry newsletter, *Inside Mortgage Finance,* and the following articles on conforming mortgages: "*Freddie offers a new A-, prepay-penalty program,*" Mortgage Marketplace, May 24, 1999; Joshua Brockman, "*Fannie revamps prepayment-penalty bonds,*" American Banker, July 20, 1999.

[23]Subprime lenders claim that borrowers voluntarily choose prepayment penalties to reduce their interest rates. Borrower choice cannot explain, however, why some 70% of subprime loans currently charge prepayment penalties and only 2% of conventional loans do (almost all in California). The real reason is that conventional mortgage markets are competitive and sophisticated borrowers have the bargaining power to avoid these fees; borrowers in subprime markets often lack sophistication or are desperate for funds and simply accept the penalty that lenders insist that they take. In addition, predatory lenders favor prepayment penalties as a way of preventing borrowers from seeking more competitive rates and terms once they realize what has happened.

[24]*See e.g.* Amy Crew Cutts, *On the Economics of Subprime Lending*, FTC Roundtable:

will deprive most borrowers of a viable way to decrease interest rates.

II. The GMPA should not be implemented without resolving its effect on TILA compliance

To ensure that the GMPA does not create havoc with compliance and enforcement of TILA, HUD should move forward on the GMPA portion of the Proposed Rule only after coordinating with the Federal Reserve Board to ensure that compliance with TILA maintains the current degree of transparency in home mortgage loans. TILA and RESPA are connected in several ways. Overhauling RESPA as suggested will create havoc to the balance currently struck between RESPA and TILA.[25]

In transactions to which RESPA applies, TILA rules say that the lender need not give an itemization of the amount financed if it provides the both the GFE and HUD-1.[26] Mortgage lenders have consistently used the GFE and HUD-1 as a replacement for the itemization of the amount financed.[27]

Economic Perspectives on the Home Mortgage Market, Washington, D.C. October 16, 2002, Slide 2.

[25]Of relevance to this discussion, TILA requires the lender to give the consumer an itemization of the amount financed, including the sum of the prepaid finance charges. However, the lender need not give the itemization if the consumer opts out of receiving it. 15 U.S.C. § 1638(a)(2)(B); Reg. Z § 226.18(c).

[26]Official Staff Commentary on Regulation Z, § 226.18(c)-4.

[27] TILA and RESPA also intersect when the mortgage transaction involves the purchase,

The importance of the consumer receiving an itemization of the closing costs for TILA compliance purposes cannot be overstated. This is the only way both regulators and consumers can determine if the APR, finance charge, and amount financed disclosures are accurate. The effect of the Proposed GMPA disclosure is to eliminate the itemization of the closing charges, at least on any form provided under RESPA. Since the HUD-1 substitutes for the TILA itemization, the effect of using the proposed truncated HUD-1 will be that neither consumers nor regulators will be able to review the TILA cost of credit disclosures for accuracy.[28]

Given the interplay between TILA and RESPA, it is imperative that HUD not move forward on implementation of the GMPA unless TILA and HOEPA compliance can be enforced.

III. <u>The GMPA rules must be tightened.</u>

If designed properly, with all of the issues relating to compliance with TILA resolved, and limited to the prime market, the Guaranteed Mortgage Package could prove helpful for consumers who shop in a competitive marketplace for their mortgages. In such a market, the GMPA would facilitate the ability of consumers to compare mortgage products that are actually available to them. With automated underwriting, mortgage lenders can (and already do in some instances) easily provide consumers guaranteed information about closing costs, interest rate and points early enough so that they can shop and make informed choices in a quick and timely manner. Only this type of inclusive disclosure would clearly meet the purposes of RESPA and offer American homeowners a real opportunity to choose the best loan available for their individual needs.

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acquisition, or construction of the home securing the mortgage. In the purchase-money context where the mortgage loan is subject to RESPA, TILA requires that a good faith estimate of the TILA disclosures be given within 3 days of application (in effect, concurrently with the GFE). 15 U.S.C. § 1638(b)(2); Reg. Z § 226.19(a)(2).

[28]HUD proposes that the HUD-1 contain a list of the finance charges that the lender used to calculate the APR. This suggestion does not cure the problems just described. Whether a particular lender violates the finance charge disclosure rules requires an independent review of all of the closing costs, not just those that the lender treated as finance charges. Under the proposal, regulators and consumers would be unable to make that independent review.

Under the current scheme of mortgage financing, very few consumers know with certainty the interest rate or the total points and closing costs they will be charged for a mortgage loan before they have to pay the fees for application, credit report, appraisal, etc. Instead, consumers must generally pay a fairly sizeable sum to apply for a mortgage loan, the full cost of which they will not know until some later time. The effect of the current industry practice is that even sophisticated consumers find it next to impossible to ensure that they are receiving the best loan that fits their needs. Moreover, unscrupulous brokers and lenders have a virtually free hand to increase the junk fees, points and/or interest rates on the loans.[29] Essentially, mortgage borrowing today is like what some folks call "buying a pig in a poke." You pay before you know what you're getting.

The better system is one in which the consumer can apply, at no charge, to the several lenders receiving the credit report, answer any additional questions the lenders request, and then receive from the lenders a guarantee of a loan at a specific rate, with a fixed amount of points charged, and a guarantee of the full amount of closing costs to be charged.[30] This guarantee should be subject *only* to two contingencies: 1) that the information supplied by the consumer regarding income and assets could be verified; and 2) that the value of the collateral -- the consumers' residence – was sufficient to secure the loan. Under this method, consumers would actually know the full price for a mortgage loan before they paid for it.

Assuming that HUD clarifies that "final underwriting" only means verification of information provided by the consumer – and requires that all of the credit qualifications of the consumer be approved *prior* to the offer of the GMPA, the GMPA should indicate the minimum requirements the consumer must meet.[31]

A. Section 8 Exemption Is Not Justified without a Clear Guarantee

Unfortunately, the Guaranteed Mortgage Package outlined by HUD in these Proposed Rules *only seems* to be describing a program like this, but the crucial elements of exactly what is promised, and what is left open to later decision – "final underwriting" – are not addressed.

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[29] The numerous class action lawsuits challenging the payment of yield spread premiums to mortgage brokers is a primary example of consumers who have found they received mortgage loans which were more expensive than they should have.

[30] All closing costs charged by the lender to close the loan would be included in this guarantee. Some expenses would be excluded from the guaranteed closing costs package, such as certain truly optional expenses like owner's title insurance, as well as expenses unrelated to the loan itself like hazard insurance and property taxes.

[31]The GMPA will be based on information provided by the consumer on income, value of home, other assets, and similar information. The preliminary underwriting performed by the lender is based on the consumer's information and the consumer's actual credit status (as determined from credit reports). However, the GMPA will be offered contingent on the consumer fitting certain preconditions, rather than needing every detail provided by the consumer to be exactly correct. For example, if the consumer provides information indicating annual income of $70,000 a year, and the terms of the loan offered in the GMPA require annual income of $60,000, the GMPA should state this. So if this consumer actually had annual income of $69,000, the GMPA should still be valid. If the consumer's information turns out to be incorrect in a *de minimus* amount, that should not alleviate the lender's obligations under the GMPA.

We have long recommended to HUD that it design a form for consumers to use when applying to lenders. Consumers could fill out this form once, and send it along with any other information a particular lender requires to a number of lenders. Each lender would then conduct a credit underwriting of the consumer's application, based on the consumer's *actual* credit, and the information provided by the consumer about income, value of the home, other assets, etc. The GMPA must then be offered to the consumer contingent only upon the lender's verification of the information provided by the consumer. Unless HUD clarifies the meaning of "final underwriting" to mean just this, the entire GMPA has minimal value for consumers – only offering lenders a way of avoiding compliance with Section 8 of RESPA, and virtually all of the important provisions of TILA.

The bottom line is that may be completely unnecessary for HUD to provide an exemption from section 8 liability to create the incentive in the marketplace to offer the guaranteed interest rate and guaranteed closing costs. There is little in current law that would stop a lender from providing these guarantees now. We do agree with HUD's principle that removing the barrier of Section 8's prohibition of volume based discounts would allow lenders to shop for settlement services and thus reduce costs. However, HUD can remove the barrier this places on the marketplace without creating the problems that will result from the exemptions from RESPA and TILA. All HUD need do is remove the current regulatory barrier for volume based discounts by requiring that the value of volume based discounts be passed along to consumers. This seems a far simpler solution than the current construct for the GMPA.[32]

B. Lender's breach of the GMPA promise must create a presumption that Section 8 has been violated

HUD must effectively hold lenders to the promises made in the GMPA. It is completely ineffective to provide that a lender's failure to keep the undertakings made in the GMPA simply causes the lender to lose the exemption from Section 8. **If the GMPA is not abided by, the consumer has no way of determining whether a Section 8 violation has occurred, and no way of alleging one in a legal complaint.** HUD must provide that a lender's failure to keep the promises made in the GMPA to the consumer results in a *presumption* of a violation of Section 8.

IV. Requirements for yield spread premiums must be tighter.

HUD has made good recommendations on how to deal with the cantankerous issue of lender payments to mortgage brokers. The Proposed Rule would amend 24 C.F.R. § 3500.7, to add a new subsection (d)(5) requiring that all yield spread premiums paid by the lender must be disclosed in the GFE as a payment to the borrower. This is very helpful to consumers – as far as it goes. However, this proposed rule change is a significant benefit to the borrower which must be included, not only in that section of the rules relating to disclosures, but also in the substantive protections of the regulations

[32] Indeed, it seems quite likely that HUD need do nothing to facilitate this type of guarantee and fixed price for closing costs. At least one large lender – ABN AMRO – has been providing this product quite successfully for some time. This lender is providing the product, with all the guarantees that we advocate (guarantee of the interest rate as well as points and closing costs) and is doing it without the exemption from section 8 liability, and with full compliance with the Truth in Lending Act. *See* www.mortgage.com. Indeed, according to one commentator, several other large lenders are now providing the same type of guaranteed packages, also without requiring a change in the law. *See,* Ken Harney, *Bundled' Settlement Fees Attracting Rate Shoppers,* Washington Post, Real Estate Section, February 10, 2003. www.washingtonpost.com/wp-dyn/articles/A8995-2003Feb14.html.

interpreting RESPA's section 8,[33] that is, in 24 C.F.R. § 3500.14.

HUD's Proposed Rule on the treatment of yield spread premiums would really be helpful if it were *not* couched entirely in the context of a disclosure. There is no private right of action under RESPA for violating its disclosure provisions.

Consumers who do business with mortgage brokers generally have the understanding that the brokers will provide them the loan at the lowest rate that the broker finds for them. Consumers have generally understood and agreed to a specific broker's fee to be paid directly by them – either in cash or by borrowing more – to the mortgage broker to compensate the broker for obtaining the loan. What consumers do not understand, and have not agreed to, is the mortgage broker receiving an additional fee from the lender. Extensive academic analysis has proven this observation to be true.[34]

As the Secretary has indicated, the goal is to change the current practices of allowing yield spread premiums to operate simply to increase the profit of mortgage brokers and lenders while providing little or no benefit to consumers. Given the statements of the Secretary, and the extensive testimony at the 2002 Senate Hearings,[35] the lack of correlation between the fees paid to a mortgage broker on a given loan and the amount of work performed by the mortgage brokers on that loan should be an accepted fact at this point. However, for HUD to make the Secretary's promise[36] a reality, several more decisive steps must be taken.

- HUD must *substantively* change the regulations regarding payments of the yield spread premium, not just the sections relating to disclosures.
- Before any payment is made to the broker, the borrower and the mortgage broker must enter into a *binding fee agreement* regarding the total compensation, however denominated, to be paid to the broker.
- The borrower must be offered a choice of how to pay the broker fee, whether in cash, by borrowing more, or by increasing the interest rate and having the lender pay the broker fee.
- This choice should be offered after loan approval but before the settlement.
- The amount the broker is paid must be the same whether paid by the borrower or the lender. The

[33]Reg12 U.S.C. X §3500§ 2607(a); 24 C.F.R. § 3500.14(b).

[34] *See, e.g.* Statement of Prof. Howell E. Jackson, Harvard Law School, before the U.S. Senate Committee on Banking, Housing, and Urban Affairs, Jan. 8, 2002, *available at* http://banking.senate.gov/02_01hrg/010802/jackson.htm.

[35]*See* Hearing on "Predatory Mortgage Lending Practices: Abusive Uses of Yield Spread Premiums." January 8, 2002. http://banking.senate.gov/02_01hrg/010802/index.htm .

[36] Regarding this new rule, the Secretary said: "The new policy will make clear that it is illegal for a settlement service provider to mark-up fees when it is making a payment to another settlement service provider, unless it provides additional value to the homebuyer in the process, or when a provider does no work for the fee and charges an unreasonable amount." *See* HUD No. 01-105, October 15, 2002, "Martinez Moves to Protect Homebuyers; Calls for Simplified Mortgage Process."

amount paid the broker by the lender reduces, by the exact amount, the amount owed by the borrower to the mortgage broker.

- The total amount paid by borrower and lender must be reasonable compensation for goods, services and facilities actually provided.

These principles accomplish several things. First, the consumer knows upfront how much the mortgage broker will charge. Second, the consumer is given the opportunity to choose how this payment will be paid. Third, and most importantly, the broker compensation remains the same regardless of method of payment. This point is crucial, because it eliminates any anti-competitive incentive the broker has to place the borrower in a loan with an interest rate greater than that for which the borrower would otherwise qualify. In other words, whether the borrower chooses a below par loan, a par loan, or an above par loan with a yield spread premium, the broker compensation will remain the same. This is not how the system works today and it must be changed.

HUD's current proposal on how to treat yield spread premiums is a variation of these principles. However, as currently configured, they are neither clear enough to offer real protections to consumers, nor are they enforceable by consumers. For example, under the new proposal it is not at all clear how and when the consumer actually exercises the choice of whether to *use* the yield spread premium. The proposed information to be included in the GFE does not necessarily include loan terms which are actually available to the consumer. It is not clear how the consumer should indicate the choice actually made.

We strongly recommend that HUD make good on the Secretary's promises and make the yield spread premium a useable – and enforceable – credit for the consumer. This can best be done by requiring two separate agreements to be executed between the consumer and the broker, one at the beginning of the relationship in which the broker states the total amount of compensation to be received for the loan, and another when the loan has been approved in which the consumer is informed of the various options by which he/she can pay the broker's fee and other closing costs, and the consumer exercises that option.

To date, yield spread premiums are generally paid by the lender to the broker solely in compensation for the higher rate loan. In other words, because the broker brings to the lender a loan at a higher rate than the consumer would otherwise qualify the broker is paid a fee, or kickback. These fees are an extra fee that the broker is able to extract from the deal. In most cases, the borrower is not only paying an upfront broker fee, but is also paying a higher interest rate as a result of this kickback. As this practice clearly provides an incentive for brokers to obtain above par loans for consumers, the dynamics of the marketplace closely resemble the marketplace that Congress attempted to control with its passage of RESPA. This is what is going on in the marketplace today, and this is why the rule proposed by HUD is so sorely needed.

Because of extensive litigation flowing from the industry's continued refusal to comply with the mandate of RESPA, in 1998, Congress issued a directive to HUD to write a Statement of Policy.[37] Despite the issuance of the 1999 Policy Statement, the industry continued as before – lenders continued to pay broker fees without evaluating either the services provided by the broker or whether the payment of

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[37]"The conferees expect HUD to work with representatives of industry, Federal agencies, consumer groups, and other interested parties on this policy statement." See the Conference Report on the Departments of Veterans Affairs and Housing an Urban Development, and Independent Agencies Appropriations Act, 1999, H.R. Conf. Rep. No. 1050769 at 260 (1998).

the lender fee reduced the fees otherwise owed by the borrower. Because the benefit to the brokers and lenders was so great (higher fees for brokers, higher interest rates for lenders), the mortgage industry's strategy was to continue its illegal practice, pay off the few individual actions brought against it and mount a massive effort to fight class action cases challenging the payment of these fees, which might actually cost the industry real money and cause the industry to change its behavior.

Despite industry's behavior, the Eleventh Circuit ultimately held that consumers could join together in class actions and challenge this activity.[38] The industry reacted strongly to this case (*Culpepper II*) and pushed HUD to step in to clarify its policy statement. HUD accepted the invitation and issued its second policy statement on the subject on October 18, 2001. The crux of HUD's "clarification" comes on page 11, with the statement:

> HUD's position is that in order to discern whether a yield spread premium was for goods, facilities or services under the first part of the HUD test, it is necessary to look at each transaction individually. . .[21]

In addition, HUD explicitly repudiated the decision in *Culpepper II* and stated its standard to be: the total compensation paid to the broker from any source (not just the lender-paid fee) must be for goods, services, or facilities. Unfortunately, the effect of HUD's 2001 Policy Statement had the intended impact on the payment of lender paid broker fees. Providing the "clarification" of the 1999 Statement as sought by the mortgage industry has had the effect of completely eliminating class actions as a form of redress for illegal lender paid broker fees.[39] Now, without class actions as a means to litigate the legality of these fees, the industry has no incentive to change its practices or even to comply with a new regulation – because there are insufficient legal resources in this nation to represent consumers in individual actions involving claims of only a few thousand dollars.

V. **The new rules for the GFE, while basically good, must be tweaked to be fully protective of consumers.**

We applaud the bright line rules proposed by HUD to severely limit the gaming currently rampant in the marketplace on closing costs. The GFE should be a true reflection of actually anticipated costs, not an opportunity for lenders to mislead consumers – as it is currently. Lenders who make numerous loans do have the capacity to determine their own charges and those of settlement service providers that they choose and require.

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[38] *Culpepper v. Irwin Mortgage Corp.*, 253 F.3d 1324 (11th Cir. 2001).

[39] This has been the exact decision of several courts, including *Glover v. Standard Fed. Bank,* 283 F. 3d 953 (8th Cir. 2002); *Shuetz v. Banc One Mortgage Corp.*, 292 F.3d 1004 (9th Cir. 2002); *Heimmermann v. First Union Mortgage Corp.,* ___ F.3d ___, 2002 WL 31067330 (11th Cir. Sept. 18, 2002).

There are a number of significant changes, however, which must be made to the construct of the proposed GFE, for example –

- The language regarding the broker's relationship to the consumer is incorrect in many states and must be deleted.
- The comparison chart on the GFE form should be uniform and reflect actual terms available to the consumer.
- There is no longer any justification to exclude home equity lines from RESPA coverage, so the rules should require they be covered.
- The disclosures in section II of the GFE should include critical loan terms such as prepayment penalties and balloon terms.
- The credit from the lender must *not* appear simply as a credit against closing costs, rather it should appear as a cash credit in the 200 series of the HUD-1.

We have provided more detailed information about our recommendations in the comments submitted to HUD.

VI. <u>There must be effective enforcement mechanisms for an originator's failure to comply with all aspects of these new rules.</u>

Even perfect consumer protection rules will only work in the marketplace if they are enforced in a meaningful way. Lenders must have incentives to comply with the rules, because lack of compliance is too costly. The Proposed Rule does not currently include *any* mechanisms to punish transgressors. The proposal only provides that once the transgression is caught, the remedy is for the lender to provide what was promised all along. This rewards *lack of compliance* because the cost of being caught breaking the rules is the same as compliance. This is frankly absurd. HUD must provide a means to make it cost originators if they violate these rules – or else the rules are virtually meaningless. We propose several specific measures to make the new RESPA rules meaningful:

- Civil enforcement of each element under the rule is essential. This includes the requirements for treatment and disclosure of the yield spread premium, the new rules for the Good Faith Estimate, as well as for a lender's failure to keep the promises in the GMPA.

- HUD must remove its stated prohibition against enforcing violations of section 8 through class actions. The 2001 Statement of Policy explicitly requires a court's individual review of each transaction, eliminating the efficient enforcement mechanism of class actions. Once HUD's Proposed Rules provide the new rules of the road, there is no reason a court cannot evaluate and enforce the yield spread requirements in class reviews – as the only issue will be whether the mortgage broker actually gave the consumer the full benefit of the payment from the lender.

- A lender's failure to follow the rules for the new Good Faith Estimate must be actionable in some manner, other than merely regulatory enforcement – as regulatory enforcement has shown that it is not sufficient to encourage the industry to comply with the law. Although the RESPA statute does not provide a private right of action in this regard, HUD can and should articulate that it believes the failure to comply with these rules is unfair and deceptive. This should enable some private enforcement under state and federal prohibitions against unfair and deceptive acts and practices.

A lender's failure to follow the rules when offering a GMPA or to close on a loan thereafter that does not conform to the GMPA must presumptively violate RESPA's Section 8. The current proposal results in the lender losing its exemption from Section 8 coverage and only allows the consumer a potential contract action against the lender for not keeping the promises in the GMPA. This is completely ineffective. As attorney's fees are generally not available for breach of contract, few consumers will have the means to bring a case to court for the few thousand dollars which would be obtained in a contract action on most failed GMPAs. Further, consumers will not have the means to allege a *prima facie* case of a violation of Section 8 as the GMPA scenario dictates that neither the initial estimate, nor the HUD 1 will provide details on the payments of fees for services provided by third parties. Therefore, HUD must state that if a lender fails to comply with the promises made in the GMPA, there is a *presumption that the lender has violated Section 8.*

Conclusion

Given the complexities of the mortgage closing process, the potential effect of the changes in RESPA's rules on predatory lending we have extensive and detailed concerns on every aspect of the HUD's proposed rules on RESPA. For a full explanation of all these concerns we respectfully refer you to our comprehensive comments filed with HUD.[40]

We have met several times with officials from HUD and we appreciate their willingness to hear our concerns and proposals. We remain seriously concerned, however, about the effect of the final changes in the RESPA rules on the low and moderate income homeowners who are already facing massive problems in the mortgage marketplace. We are hopeful, however, that HUD will attend to these issues and not exacerbate the crisis situation facing this nation's communities.

Thank you for the opportunity to testify today.

[40]These comments are available on NCLC's website at www.consumerlaw.org.

Testimony of

America's Community Bankers

on

Simplifying the Home Buying Process:
HUD's Proposal to Reform RESPA

before the

Subcommittee on Housing and Community Opportunity

of the

Committee on Financial Services

of the

U.S. House of Representatives

on

February 25, 2003

D. Russell Taylor
President and CEO
Rahway Savings Institution
Rahway, New Jersey

and

Chairman
America's Community Bankers
Washington, DC

Good afternoon. Chairman Ney, Ranking Member Waters, Distinguished Members of the Committee, thank you for the opportunity to testify at today's hearing on the Department of Housing and Urban Development's proposed rule on the reform of the Real Estate Settlement Procedures Act implementing regulation.

My name is D. Russell Taylor, President and CEO of The Rahway Savings Institution in Rahway, New Jersey. In addition, I am the Chairman of America's Community Bankers. America's Community Bankers represents the nation's community banks of all charter types and sizes. ACB's member banks originate more than 25 percent of all mortgages in the United States, and significantly more than half of all mortgages originated by depository institutions. In addition, ACB members operate a large number of mortgage banking affiliates that originate a substantial part of the business for that segment of the industry.

The Rahway Savings Institution is a New Jersey chartered mutual savings bank with $375 million in assets. As one of New Jersey's oldest financial organizations, it has endured the Great Depression of the 1930's and remained a stronghold throughout the troubled period for banking in the 1980's. We take great pride in the fact that we are local enough to provide personalized attention to our customers, but large enough to offer them the wide range of banking products and services they need. We look forward to serving all of our customers' financial needs--which includes an integral role in providing access to homeownership.

Homeownership is important to every member of America's Community Bankers. The nation's homeownership rate was a record 67.9 percent in 2002, up from 67.8 percent the year before. Last year, the African American homeownership rate increased to 47 percent and the Hispanic homeownership rate increased to 48 percent. ACB members are working hard to increase homeownership rates across the country, which first begins with our lenders financing mortgages.

Mortgage finance is a primary business line of the majority of ACB members.
We have members who sell all of their loan originations into the secondary market, members who retain all loans originated in portfolio, and members who do both. Because the membership is nationwide, many members are subject to local laws and regulations that may conflict with elements of HUD's proposal. Any changes to the disclosures or to any aspect of compliance with RESPA will have a significant impact on the business of ACB member institutions.

ACB has been an active advocate of and participant in the mortgage reform debate. We welcome changes to the current disclosures that will provide consumers with a measure of certainty and clarity, because we must increase the homeownership rate so that ALL Americans will be able to own a home, if they so choose.

For this reason, ACB welcomes the opportunity today to comment on the proposal issued by HUD to amend Regulation X, the regulation implementing RESPA.

ACB commends HUD's efforts to reform the mortgage process. Secretary Martinez and the HUD staff should be applauded for taking this important first step to amend the regulation and required disclosures. We appreciate that some of our earlier suggestions have been reflected in the proposal. ACB believes that current requirements are extremely burdensome and do not provide consumers with information that is easily understood or as useful as it might be. The compliance burden of current regulations is very high and any change will require costly and time-consuming modifications to systems and operations.

Although any new regulation also likely will be costly and burdensome for lenders, we hope that ultimately this regulation will reduce costs for consumers and lenders alike. However, insured depository institutions subject to examination and supervision will be required to comply quickly and accurately. As a result, ACB asks for a sufficient transition period for the implementation.

Summary

ACB offers the following specific suggestions, which we believe will make the rule more workable for all industry participants, while fulfilling HUD's goals and the principles established by the Secretary.

On the three areas of the proposal, ACB generally supports the concept of the Guaranteed Mortgage Package and the concept of requiring mortgage broker disclosures. However, we strongly urge HUD to reconsider making changes to the Good Faith Estimate contemporaneously with introduction of the Guaranteed Mortgage Package. We believe that making all of these changes at the same time would unnecessarily disrupt the mortgage market.

We would like to make the following additional comments.

- The proposed mortgage broker disclosures are necessary for consumers to understand the manner in which brokers receive compensation for services provided. Providing this information is essential to decision-making and should be part of any financial literacy efforts;

- HUD must include a reasonable transition period in any changes that are made;

- There are a number of consumer protection laws that contain requirements that are duplicative of or conflict with the proposal. In particular, proposed RESPA changes must be coordinated with Truth in Lending Act requirements;

- HUD must work with the federal banking agencies to ensure that supervision, examination and accounting concerns can be addressed without adversely affecting the ability of insured depositories to offer mortgage products; and

- RESPA must be enforced vigorously by HUD uniformly across affected institutions.

Mortgage Broker Disclosures

ACB believes that the addition of mortgage broker fee disclosures is an important element of mortgage reform. We support HUD in its efforts to require this disclosure and we do not believe that potential delays in other elements of the proposal should result in a delay in requiring this disclosure. Fees charged by mortgage brokers are frequently misunderstood by consumers. We urge HUD to include an easy to understand mortgage broker disclosure requirement in any final rule that is issued.

ACB and other groups in the mortgage-lending arena sent a letter of support for improved fee disclosures after the issuance of the statement of policy in October 2001. As part of that letter of support, ACB and other organizations suggested a method of requiring mortgage broker disclosures. A copy of the letter and the suggested model disclosure form are in the appendix to this written statement.

The Guaranteed Mortgage Package and the Good Faith Estimate of the proposal must be separated

ACB supports the option of the Guaranteed Mortgage Package but we strongly believe that the current good faith estimate must remain an alternative for those lenders who do not wish to package or are unable to do so. As important as it is that consumers be able to comparison shop for mortgage credit, lenders must be able to offer an array of products to meet varying needs of the customer and to give consumers disclosures that are meaningful.

Most importantly, ACB believes that small-to medium-sized lenders are an integral part of the mortgage process and that it is imperative that they be able to be a part of the packaging option to the extent they wish. We believe that many community banks will be able to work with third parties in their local communities to offer an attractive package.

However, it may be that the optimal way for smaller institutions to participate in the packaging option may be for a third party to coordinate, subcontract or otherwise negotiate and arrange the Guaranteed Mortgage Package. We believe that the exemption from Section 8 liability should extend to the activities currently permitted pursuant to HUD's policy.

If the Guaranteed Mortgage Package succeeds, it will be because the market is ready for such an alternative and it is found to be a meaningful shopping tool by consumers. The experiment also will succeed if lenders and other companies are able to put together packages in an efficient and cost effective manner. However, given the vast array of mortgage products, even those lenders who package may not be able to provide all of the options that consumers need. Each of these concerns may limit the viability of the Guaranteed Mortgage Package. The only fair way to determine if it will work is to try the alternative, while allowing lenders who do not wish to package to use the current mortgage origination process.

ACB strongly believes that implementing the Guaranteed Mortgage Package, while attempting to significantly change Good Faith Estimate procedures at the same time, would create undo stress on the mortgage markets.

Guaranteed Mortgage Package

The proposed Guaranteed Mortgage Package arguably would provide consumers the easiest method of comparison-shopping because it will require a lump sum price for all loan originator and governmental required settlement costs associated with obtaining a mortgage, combined with a "so-called" interest rate guarantee for the loan.

However, we are concerned that providing a "so-called" interest rate guarantee that is held open for a minimum of 30 days as part of the package, would not work. We understand that the rate may move based on an index or other observable market changes, but requiring an interest rate guarantee of this sort may lead to confusion on the part of the consumer. The lender will have to develop a method of establishing the rate and determining whether it will change in a manner that will be easily understood by the consumer so that he or she can assess the comparative benefit of the package as time goes on until the rate lock occurs. We suggest that HUD work with lenders of all types to develop a methodology for establishing and adjusting rates. It is important that all types of mortgage lenders be part of this discussion. Some large mortgage lenders maintain or use a readily recognizable index, but smaller lenders or those that retain loans in portfolio may not have an easily understood index.

This concern is exacerbated by the length of time the Guaranteed Mortgage Package is to remain open. The proposal requires the offer to remain open for a minimum of 30 days. We believe that this period of time is much too long. Most home purchase contracts require that financing be applied for within five days.

Another concern is that of conflicts with state law. There are approximately 40 states in which the Guaranteed Mortgage Package may not be able to be implemented for a variety of reasons. We are aware that some of the services to be provided in the package are not permitted by some of the entities that HUD and industry participants envision may become packagers. For example, in some states mortgage brokers are not permitted to give documents containing the annual percentage rate. Also, there are states that have state RESPA and Truth in Lending statutes that must be considered. In my state, New Jersey, borrowers have a right to select the settlement attorney of their choice, possibly upsetting the packaging approach. ACB suggests that HUD look at the differences in how closings are conducted from state to state, and at what different state laws may require. We understand that the method of delivering title insurance and other services varies from state to state. This has an impact on the cost and timing of delivery of the product.

Finally, we agree that entities other than lenders should be able to package and obtain an exemption from Section 8 liability. However, careful consideration must be given to restrictions on the ability of government sponsored enterprises to offer such packages, and whether regulations to prevent loan steering by third party packagers are necessary. Without such restrictions and regulations, the full competitive benefits of RESPA reform are unlikely to be enjoyed by consumers. Further, such regulations may be necessary to prevent an unintended consequence of business being steered away from community lenders.

Good Faith Estimate

The proposed GFE raises a host of compliance and operational difficulties that require significant review and revision before it can be implemented. The changes to the GFE contained in the proposal are sufficiently sweeping that lenders will have to change everything about the way they provide disclosures, resulting in a drastic increase in regulatory burden. If the proposal were finalized as currently drafted, lenders would have the opportunity to offer the guaranteed package, but if they elected not to or were unable to do so, they would still have to change their processes to accommodate the wholesale changes to the GFE.

Additional Concerns of the Proposal

Extended Transition Period Required

An extended transition period of a minimum of several years would be required for many parts of the HUD proposal. The creation of a Guaranteed Mortgage Package will not require such a lengthy phase in period, but it may take that amount of time to resolve some of the state law conflicts. If the GFE is adopted in the proposed form, the transition time required to ensure compliance would be a minimum of two to three years. Lenders would have to amend their requirements, train staff, and check the quality of the disclosures.

Changes must be coordinated with other federal banking agencies

Both the proposed Guaranteed Mortgage Package and the proposed revisions to the GFE contain changes that must be coordinated with the requirements and the definitions of other consumer protection laws that are implemented by regulations promulgated by the Federal Reserve. The most important example of a regulation that must be coordinated with these proposed requirements is Reg Z, the regulation that implements the Truth in Lending Act, and the disclosures required under that regulation. Both the proposed GFE and proposed GMPA require that the APR be disclosed, an element of disclosure required by the Truth in Lending Act. Much of the information required by the proposal is already required by TILA. Currently, the TILA disclosures are given at the same time as the GFE.

The purposes of Truth in Lending and RESPA are different. TILA was enacted to provide consumers with the cost of credit, and RESPA was enacted to provide the costs of settlement. The disclosures required by and definitions used in TILA and RESPA must be coordinated or consumers will be confused by documents that they receive at the same time.

Supervision, Examination and Accounting Conflicts with Federal Banking Agencies

An unintended consequence of the guaranteed rate requirement contained in the Guaranteed Mortgage Package and the proposed GFE is that there may be supervisory or accounting concerns about the treatment of these guaranteed rates. HUD must consult with both accounting standard setters and federal bank regulatory agencies with respect to the guaranteed rate in the Guaranteed Mortgage Package and the GFE. The agencies' analysis of a regulated banking institution may very well be affected by the rate guarantee provision in the proposal, especially in relation to the interest rate sensitivity of the institution in much the same way that agencies would consider a formal loan commitment.

Laws and Regulations Should be Enforced Vigorously

We urge HUD to strengthen its review and enforcement program of lenders who are not otherwise examined and supervised. ACB member institutions are insured depository institutions subject to regular supervision and examination. Examinations include reviews of their policies and procedures, as well as specific transactions.

Financial Literacy is an Important Element of Mortgage Reform

We strongly believe that consumers who know and understand what they are shopping for are the best homebuyers. We believe that education must begin before the consumer makes an application. Homeownership counseling is a crucial step to purchasing a home. According to community bankers responding to ACB's 2003 Real Estate Lending Survey five to ten percent of community bank loan production is made up of first-time homebuyers, and 64 percent of ACB's members have either required or recommended education and counseling for at least one mortgage or consumer lending product. Education can increase the number of potential borrowers, and counseling can mitigate credit problems.

Conclusion

ACB strongly supports mortgage reform and believes that HUD's proposed RESPA changes are a good start. In order for consumers to benefit from RESPA reform, the rules have to be realistic and workable in the marketplace.

We urge HUD to implement in a timely manner mortgage broker fee disclosures, and separate the implementation of the Guaranteed Mortgage Package from the revised Good Faith Estimate. Mortgage broker fee disclosures are an integral part of making mortgage fees comprehensible to consumers, which is essential to financial literacy efforts. The Guaranteed Mortgage Package, with revisions, should take priority and be tested in the market as soon as practicable. Revisions to the Good Faith Estimate should be postponed, reexamined and adjusted as the Guaranteed Mortgage Package is being tested.

In order for a final rule to be implemented effectively, concerns and conflicts with other federal regulators and banking agencies must be reconciled. Similarly, HUD must address the existence of state laws that frustrate the underlying purpose of the packaging concept. We encourage HUD to apply the safe harbor exemption to HOEPA loans.

ACB members stand ready to work with Members of the Committee and HUD to complete the RESPA reform process in a way that is efficient and feasible.

Thank you for the opportunity to express the views of members of America's Community Bankers.

Appendix to Testimony of

America's Community Bankers

on

Simplifying the Home Buying Process:
HUD's Proposal to Reform RESPA

before the

Subcommittee on Housing

of the

Committee on Financial Services

of the

U.S. House of Representatives

on

February 25, 2003

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October 28, 2002

Rules Docket Clerk
Office of General Counsel, Rm. 10276
Department of Housing and Urban Development
451 Seventh Street, S.W.
Washington, D.C. 20410-0500

Re: Real Estate Settlement Procedures Act (RESPA);
Simplifying and Improving the Process of Obtaining
Mortgages to Reduce Settlement Costs to Consumers
Docket No.: FR-4727-P-01
67 FR 49134 (July 29, 2002)

Dear Sir or Madam:

America's Community Bankers ("ACB")[1] welcomes the opportunity to comment on the proposal issued by the Department of Housing and Urban Development ("HUD") to amend Regulation X, the regulation implementing the Real Estate Settlement Procedures Act ("RESPA").[2] The objective of the proposal is to simplify and improve the process of obtaining home mortgages and reduce settlement costs for consumers.

The necessity for changes to the disclosure requirements results from a number of factors. The mortgage market has changed substantially since the regulation and the disclosures were adopted several decades ago. HUD and the Federal Reserve issued a report[3] in 1998 as part of which the disclosures were reviewed. A number of issues and concerns were raised as part of this study, but no changes have been made as a result of the issues raised. In fact, the market place continues to evolve at a rapid rate and access to technology and development of new products make changes more important.

The proposal seeks to simplify and improve the mortgage process in several respects: first, the issue of loan originator disclosure would be addressed; second, changes would

[1] ACB represents the nation's community banks of all charter types and sizes. ACB members, whose aggregate assets exceed $1 trillion, pursue progressive, entrepreneurial and service-oriented strategies in providing financial services to benefit their customers and communities.
[2] 67 Fed. Reg. 49134 (July 29, 2002)
[3] Joint Report to the Congress Concerning Reform of the Truth in Lending Act and Real Estate Settlement Procedures Act (July 1998)

be made to the good faith estimate settlement cost disclosure; and the regulatory barriers to allow guaranteed packages of settlement services and mortgages would be eliminated. Each of the elements of the proposal is very detailed and complicated, as is often the case when a proposal is issued to change a disclosure regime that has been in place for 25 years. In early October, ACB requested a meeting with HUD staff to discuss some of the details of the proposal and we are awaiting a response from HUD staff. We respectfully request that we be permitted to submit additional comments after we have had the meeting with HUD staff, which we are hopeful will occur in the near future.

ACB Position

ACB generally supports HUD's efforts to amend the regulation that implements RESPA to accomplish mortgage reform. The Department is to be commended for taking this important first step to amend the regulation and the disclosures.

However, we have reservations about the practical application of the changes as proposed. Many of the disclosure requirements have not been amended in over 25 years and major changes have taken place during this time in the mortgage market and the mortgage origination process. Mortgage brokers have become an important participant and the secondary market for mortgage loans has been developed so that sales of loans into the secondary market are commonplace.

In the preamble to the proposed rule, HUD acknowledges that the American mortgage finance system is the envy of the world.[4] While ACB supports HUD in its efforts to bring the mortgage origination process into the 21st century and, at the same time, ensure that consumers are given accurate and timely disclosures on which to base decisions, we urge HUD to amend the proposal as suggested below and to move cautiously to issue a final rule so that the market can absorb the changes with out lapses in compliance and the ever present threat of litigation. We urge HUD to work with industry participants to develop a rule that preserves the best features of a successful mortgage finance system.

ACB offers the following suggestions, which we believe will make the rule more workable for all industry participants, while fulfilling HUD's goals and the principles established by the Secretary. On the three areas of the proposal, ACB generally supports the concept of the Guaranteed Mortgage Package and the concept of requiring mortgage broker disclosures. However, we strongly urge HUD to reconsider making any changes to the Good Faith Estimate ("GFE") at this time. We believe that making all of these changes at the same time would unnecessarily disrupt the mortgage market.

- HUD must divide the proposal into more manageable pieces, rather than issuing a final rule that would simultaneously change every aspect of the mortgage origination process. We suggest that HUD amend the proposed Guaranteed Mortgage Package and reconsider the proposed changes to the GFE.

[4] 67 Fed. Reg. 49134

- While we support the Guaranteed Mortgage Package, we suggest a number of amendments that must be made to ensure this alternative is truly viable for all lenders;

- The proposed changes to the GFE are not a workable option in the current form. We question HUD's authority to make some of the changes. We suggest that HUD delay these proposed changes and take the time to study the issue as well as better state the legal authority, which would permit such changes. We strongly urge HUD to repropose this piece of the proposal after taking the comments into account;

- HUD must include a reasonable transition period in any changes that are made;

- There are a number of consumer protection laws that contain requirements that are duplicative of or conflict with the proposal. HUD must work with the other agencies, especially the Federal Reserve, to ensure that the requirements of other consumer protection laws are met and that the requirements are not in conflict;

- HUD must work with the federal banking agencies to ensure that supervision, examination and accounting concerns can be addressed without adversely affecting the ability of insured depositories to offer mortgage products;

- Mortgage broker disclosures must be included in any final rule;

- It is essential that any new forms be tested with consumers to ensure that they are understandable. ACB would be pleased to work with our members and their customers to have them assist in HUD's testing effort. The testing should include education and a transition period;

- RESPA must be enforced vigorously by HUD uniformly across affected institutions;

- The secondary market housing government sponsored entities should not be permitted packagers; and

- A strong emphasis on financial literacy must be included in any initiatives.

General

Mortgage finance is a primary business line of the majority of ACB members. Savings institutions, which compromise a large percentage of ACB's membership, originate a quarter of all mortgages made in this country. Any changes to the disclosures or to any aspect of compliance with RESPA will have a significant impact on the business of ACB member institutions. We have members who sell all of their loan originations into the secondary market, members who retain all loans originated in portfolio, and members who do both. The product offerings of ACB members vary as well in order to meet the needs of the communities they serve. Because the membership is nationwide, many members are subject to local laws and regulations that conflict with elements of the proposal.

ACB has been an active advocate of and participant in the mortgage reform debate. We welcome changes to the current disclosures that will provide consumers with a measure of certainty and clarity.

Nevertheless, we have serious reservations about whether the current proposal, in its entirety, will accomplish the goals established by HUD or comply with the principles set forth by the Secretary when he announced the issuance of the proposal. We believe that separate elements in the proposal, if amended, are worthy of continued review and encourage HUD to work with the industry to finalize them.

The major elements of the proposal must be separated

As an initial matter, ACB welcomes the proposal as a first step in amending the disclosure regime. For years industry participants have met with HUD, with each other and with consumer groups to try to develop changes to the mortgage process on which everyone can agree. We agree that consumers must be given early disclosures that accurately reflect the cost of credit so that they can comparison shop in a meaningful way. However, this proposal seeks to radically change every aspect of the mortgage process without the benefit of knowing whether some of the changes are workable. ACB supports the option of the Guaranteed Mortgage Package but we strongly believe that the current good faith estimate must remain an option for those lenders who do not wish to package or are unable to do so. As important as it is that consumers be able to comparison shop for mortgage credit, lenders must be able to offer an array of products to meet customers varying needs and give consumers disclosures that are meaningful.

If the Guaranteed Mortgage Package succeeds, it will be because the market is ready for such an option and it is found to be a meaningful shopping tool by consumers. No one can predict whether consumers will shop for a mortgage using this approach. The experiment also will succeed because lenders and other companies are able to put together packages in an efficient and cost effective manner. It may be that only certain lenders will see this as a viable option. Also, given the vast array of mortgage products, even those lenders who package may not be able to provide all of the options that consumers need. Each of these concerns may limit the viability of the Guaranteed Mortgage Package. The only fair way to determine if it will work is to try the alternative, while allowing lenders who do not wish to package to use the current mortgage origination process.

HUD points out that one of the industry segments most interested in the Guaranteed Mortgage Package option are the large lenders.[5] ACB believes that small-to medium-sized lenders are an integral part of the mortgage process and that it is imperative that they be able to be a part of the packaging option to the extent that they wish. The only way that smaller institutions may be able to participate may be for a third party to coordinate, subcontract or otherwise negotiate and arrange the Guaranteed Mortgage Package. We believe that the safeharbor should extend to the activities currently permitted pursuant to HUD's policy.[6]

We strongly urge HUD to move ahead to complete and implement the package option. However, changes to the GFE should be postponed and reexamined at a later date. We suggest that making both changes at the same time would create undo stress on the mortgage markets. In addition, as will be described more fully below, we do not believe that the proposed changes to the GFE are practicable. We would welcome the opportunity to work with HUD to develop a more workable option.

Guaranteed Mortgage Package

The proposed Guaranteed Mortgage Package would contain a lump sum price for all loan originator and governmental required settlement costs associated with obtaining a mortgage, combined with an interest rate guarantee for the loan. The packager would offer a lump sum price for settlement costs and an interest rate guarantee at no cost to the borrower until the borrower selects the package; the packager would be held to those figures from the time the package is agreed to through closing. HUD believes that this method would enable consumers the easiest method of comparison-shopping.

In concept, ACB supports HUD's packaging proposal. However, we have some reservations about the details of the package as proposed. We agree that entities other than lenders should be able to package and obtain a section 8 exemption, so long as such entities comply with the requirements established by HUD.

We are concerned that providing an interest rate guarantee that is held open for a minimum of 30 days as part of the package, does not work. We understand that the rate may move based on an index or other observable market changes, but requiring an interest rate guarantee of this sort may lead to confusion on the part of the consumer. The lender will have to develop a method of establishing the rate and determining whether it will change in a manner that will be easily understood by the consumer so that he/she can assess the comparative benefit of the package as time goes on until he/she locks. We suggest that HUD work with lenders of all types to develop a methodology for establishing and adjusting rates. It is important that all types of mortgage lenders be part of this discussion. Some large mortgage lenders maintain an index or use a readily

[5] Id. at 49145
[6] Letter dated February 14, 1995, from Assistant Secretary Retsinas to the Independent Bankers Association of America. The letter provides a list of compensable loan origination services. HUD Statement of Policy 1999-01 reiterates the services.

recognizable index because of the match to the cost of funds, but smaller lenders or those that retain loans in portfolio may not have an easily understood index.

This concern is exacerbated by the length of time the Guaranteed Mortgage Package is to remain open so that the consumer may use the information to shop. The proposal requires the offer to remain open for a minimum of 30 days. We believe that this period of time is much too long. We urge HUD to reconsider this time frame and shorten the period of time during which the offer must remain open to five business days. Most home purchase contracts require that financing be applied for within five days.

Additionally, if the 30-day period is to be used for shopping by the consumer and the consumer obtains information about a package from several lenders and also obtains a GFE from several lenders, how can the comparisons be made? It appears that an assumption has been made that consumers will not try to compare the costs of the GFE with the price of the package.

Another issue that ACB is concerned about with regard to the Guaranteed Mortgage Package is that of conflicts with state law. Anecdotally, we are aware that some of the services to be provided in the package are not permitted to be provided by some of the entities that it is contemplated will be packagers. For example, in some states mortgage brokers are not permitted to give documents containing the annual percentage rate ("APR"). Also, there are states that have state RESPA and Truth in Lending statutes that must be considered. ACB suggests that HUD work with the state regulators and supervisors of entities to determine whether there are conflicts that can be resolved.

We have included additional remarks regarding the Guaranteed Mortgage Package below in the section entitled Questions for Commenters #11 – #28.

Good Faith Estimate

ACB opposes the adoption of the proposed GFE at this time and urges HUD to postpone action on the GFE until the Department has taken the time to review the GFE and to allow the Guaranteed Mortgage Package has been tested in the marketplace.

The proposed GFE raises a host of compliance and operational difficulties that require significant review and revision before it can be implemented. While the current GFE is not be without flaw, it is a workable option. The changes to the GFE contained in the proposal are sufficiently sweeping that lenders will have to change everything about the way they provide disclosures resulting in a drastic increase in regulatory burden. If the proposal were finalized as currently drafted, lenders would have the opportunity to offer the package, but if they elected not to or were unable to do so, they would still have to change their processes to accommodate the wholesale changes to the GFE.

We have concerns about whether HUD has the legal authority to finalize some of the changes proposed. We question whether the rate information and the requirement that tolerances be adhered to are contemplated by RESPA. We do not believe that such restrictions belong in a document that is to be an estimate, particularly when the disclosures required under the TILA are meant to address the cost of the credit while RESPA is meant to disclose the cost of settlement.

While HUD has clear authority to issue regulations to carry out the purpose of RESPA, we question whether HUD has the authority to impose a zero tolerance on any cost category on the GFE. We are uncertain whether HUD has the specific authority to require a full refund to the borrower if costs at settlement exceed the applicable tolerances.

ACB suggests that HUD look at the differences in how closings are conducted from state to state and at what different state laws may require. We understand that the method of delivering title insurance varies from state to state. This has an impact on the cost and timing of delivery of the product.

We also are concerned about the instances in which changes must be made due to circumstances beyond the lender's control. For example, we understand that during the mortgage process the prospective borrower may make changes or the lender discovers that information must be changed based on underwriting or an appraisal. Again, the array of products the lender offers must be considered. A consumer may request a GFE based on assumptions and the lender may discover that another loan product may be much more suitable for the borrower. In this situation, it appears that redisclosures will have to be made. This will be confusing for the consumer, and if another 30-day period is commenced, burdensome for the lender. Effective shopping will be hindered. We suggest that a method for redisclosures be developed.

Examples of operational and compliance concerns regarding the proposed GFE include (but are not limited to):

- The 30-day minimum time period in which the GFE must be valid;
- The tolerance levels;
- Redisclosure when the borrower requests a change in the mortgage terms;
- Replication of information on the GFE and the Truth in Lending statement;
- The accuracy of estimated escrow amounts at the time the GFE is issued;
- The clarity to borrowers of the form itself.

We urge HUD to clarify the proposal to address other types of loans. RESPA is applicable to a number of loan types that do not appear to be contemplated in this proposal. The proposal addresses only traditional first-lien mortgage loans. Lenders are required to disclose GFEs on second mortgage loans, commitments for permanent financing, and in some cases, on construction loans. HUD should specifically address each of these loan types and how the GFE should be prepared under the following conditions:

- Construction Loans. Typically construction loans can take anywhere from 90 days to a full year or more before the home is completed. Because they are short-term loans, many of the disclosures required on the proposed GFE do not apply. Rates and fees are not set in the same manner as they are on traditional first mortgage loans.
- Commitment for Permanent Financing or Construction-Perm loans. Lenders will often qualify a borrower for permanent financing six months to a year before the loan is actually closed. Rates are rarely locked and there is often not sufficient information to provide firm estimates of fees. In particular, the amount of property taxes is almost never known at the time of application. Clarification on how the 30 days should be handled for construction lending and commitments for permanent financing is needed.
- Consumer Home Equity Loans. The proposed GFE and Guaranteed Mortgage Packages are clearly designed for first mortgages only and would be very cumbersome for consumer home equity loans.
- Home equity loans rarely have either an "interest rate dependent payment" (discount) or an opportunity by the borrower to lock the rate.
- The options shown on the second page of the proposed GFE for payment of closing costs generally are not offered on second mortgage loans. Home equity loans are generally priced consistently for every borrower and there is no opportunity for adjusting rates based on fees.

The abuses HUD is concerned about generally do not occur for the loans listed above. Market forces generally allow few if any fees on these loans. Requiring the use of the proposed GFE for these loans would significantly increase the costs associated with making these loans and would be very confusing to consumers.

Generous Transition Period Required

The changes proposed by HUD would be sweeping changes to the mortgage origination process. To the extent that any of the elements of the proposal are adopted in final form, a generous transition period of a minimum of several years would be required. The Guaranteed Mortgage Package will not require such a lengthy phase in period, but it may take that amount of time to resolve some of the state law conflicts and other issues. If the GFE is adopted in its currently proposed form, the transition time required to ensure compliance would be minimum of two to three years. Lenders will have to amend their requirements, train staff, and check the quality of the disclosures. Finally, as will be discussed further below, several of these changes must be coordinated with one or more other federal agencies, in particular the Federal Reserve.

Changes must be coordinated with other federal banking agencies

Both the proposed Guaranteed Mortgage Package and the proposed revisions to the GFE contain changes that must be coordinated with the requirements and the definitions of other consumer protection laws that are implemented by regulations promulgated by the Federal Reserve. We strongly urge HUD to work with the staff of the Federal Reserve to ensure that the requirements are compatible, understandable, and not duplicative. We believe that if such coordination does not take place and corresponding changes made that any final rule will be virtually impossible to implement.

For example, a consumer making an application triggers the disclosure requirements of both the proposed revisions to the GFE and the Guaranteed Mortgage Package. The definition of an application is the submission of credit information (Social Security number, property address, basic income information, the house price or a best estimate on the value of the property, and the mortgage loan needed) by the borrower in anticipation of a credit decision. If the submission does not state or identify a specific property, the submission is an application for a pre-qualification and not an application.

This definition of an application is different from the definition of an application under Regulation C, the implementing regulation for the Home Mortgage Disclosure Act ("HMDA"). This difference would cause confusion for lenders filing out the HMDA loan application register. A consumer who makes an application at several lenders in order to shop for credit will get a GFE or a Guaranteed Mortgage Package agreement, which are both offers of credit. This may trigger a HMDA filing requirement. One consumer may have multiple offers outstanding and each of these offers would be reported, rather than the one transaction that occurs.

Another example is compliance with Regulation B, the implementing regulation for the Equal Credit Opportunity Act ("ECOA"). Regulation B provides a process for making a counter offer to a consumer. The proposal is not clear on what the process would be. Would the consumer receive another GFE or Guaranteed Mortgage Package Agreement and would that trigger another 30-day period? A lender may deny the credit rather than issue a counter offer.

To the extent that consumers apply for mortgages at different lenders for purposes of shopping, each lender may pull a credit report for the borrower to determine the loan product best for him/her. Multiple requests for credit reports for the same consumer often results in a lowering of the credit rating for the consumer. Thus, the consumer may have started the process with a better rating and at the beginning have been able to obtain a more advantageous loan. However, because he/she shopped at a number of lenders, the loan product received may not be as good.

The most important example of a regulation that must be coordinated with these proposed requirements is Regulation Z, the regulation that implements TILA, and the disclosures required under that regulation. Both the GFE and the Guaranteed Mortgage Package

Agreement require that the APR be disclosed. Much of the information required by the proposal is already required by TILA. The TILA disclosures are given at the same time as the GFE. The purposes of the statutes are different. TILA was enacted to provide consumers with the cost of credit and, in contrast, RESPA was enacted to provide costs of settlement. The disclosures required by and definitions used in TILA and RESPA must be coordinated or consumers will be confused by documents that they receive at the same time.

Supervision, Examination and Accounting Conflicts with Federal Banking Agencies

An unintended consequence of the guaranteed rate requirement contained in the Guaranteed Mortgage Package and the proposed GFE is that there may be supervisory or accounting concerns about the treatment of these guaranteed rates. HUD must consult with both accounting standard setters and federal bank regulatory agencies with respect to the guaranteed rate in the Guaranteed Mortgage Package and the GFE. As part of the examination and supervision responsibilities, the federal banking agencies pay close attention to insured depository institutions' exposure to interest rate risk. The agencies' analysis of a regulated banking institution may very well be affected by the rate guarantee provision in the proposal, especially in relation to the interest rate sensitivity of the institution in much the same way that agencies would consider a formal loan commitment. Such guarantees may have to be hedged in the same manner as loan commitments. In addition, the rate provision may also have GAAP accounting implications. The FASB currently has a project examining the accounting treatment of financial guarantees that may require special treatment for mortgages subject to the guaranteed rate requirement.

Mortgage Broker Disclosures

ACB believes that the addition of mortgage broker fee disclosures is an important element of mortgage reform. We support HUD in its efforts to require this disclosure and we do not believe that a delay in other elements of the proposal should result in a delay in requiring this disclosure.

Because we do not support the proposed GFE in its current form, we suggest an alternative for mortgage broker disclosures. As HUD points out in footnote 26[7] in the preamble to the proposal, ACB, along with several other organizations, sent a letter of support for improved fee disclosures after the issuance of the statement of policy. As part of that letter of support, ACB and other organizations suggested a method of requiring mortgage broker disclosures. We strongly urge HUD to consider adopting a form of mortgage broker fee agreement. A copy of the letter and the model disclosure form are attached. ACB stands ready to work with HUD to develop an alternative.

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[7] 67 Fed. Reg. 49143

Model Forms Should be Tested

As part of the proposal, HUD has included model forms for the revised GFE and the Guaranteed Mortgage Package Agreement as appendices. These forms include instructions. In the preamble to the proposal, HUD said that it intends to hold focus groups of consumers during the comment period.[8] ACB urges HUD to hold such focus groups if it has not already done so. The forms that are included in the proposal are confusing and the instructions do not add any clarity. Because one of the goals of this proposal is to provide consumers with meaningful disclosures with which they may shop, we believe that the disclosures should be tested by a wide variety of consumers from different economic, geographic, and educational backgrounds. It is also important that HUD test these forms, while showing the consumer the other forms that he/she will receives as part of a mortgage. The consumer must see that the GFE is given with TILA disclosures and other HUD disclosures. That is the only way that HUD will be able to determine whether the disclosures will meet the stated goals and are not duplicative and confusing. These forms cannot be finalized without coordinating all of the forms given as part of the process.

Further, HUD mentions that it will revise the required information booklet as part of this process. We suggest that revisions to this document can include much of the explanatory information HUD currently includes in the forms and instructions. We urge HUD to use this opportunity to make the booklet an educational tool that explains the process and who the players are. Again, we reiterate our offer to have ACB members participate in testing.

Laws and Regulations Should be Enforced Vigorously

One of the principles announced by the Secretary as part of this rulemaking is that RESPA should be vigorously enforced to protect borrowers and ensure that honest industry providers have a level, competitive playing field. ACB agrees with this principle. As we have discussed, ACB institutions are insured depository institutions subject to regular supervision and examination. Examinations include reviews of their policies and procedures, as well as specific transactions. If any of the abuses that HUD seeks to address in the proposal are discovered through routine examination, they can be resolved. We urge HUD to strengthen its review and enforcement program of lenders who are not otherwise examined and supervised.

Housing GSEs Should not be Permitted Packagers

The proposal contemplates that entities other than lenders may qualify as packagers so long as the package includes a mortgage and the entity otherwise satisfies the requirements of the safe harbor. ACB strongly urges HUD, in its role as the program regulator for the housing secondary market government sponsored enterprises ("GSE") to

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[8] Id. at 49148

clarify in any final rule that the GSEs are not permitted packagers. We do not suggest that a variety of companies should be excluded for being packagers. In fact, we believe that for the Guaranteed Mortgage Package option to work, entities of all types should be able to provide the package. We believe that this is the only way that small to medium sized lenders and other settlement companies will be able to take advantage of the opportunity. However, we believe that the secondary market housing GSEs should not be able to provide an option that we believe is a function of the primary market.

ACB has a policy position on the activities of the GSEs that has been developed over time. We believe that these entities should limit their activities to those that are permissible pursuant to their chartering documents. These activities only should be pursued to the extent that they are compatible with secondary market activities. We believe that packaging is a primary market activity and therefore not a permitted activity for the GSEs. Given the business and operations incentives of the GSEs and the development of automated underwriting systems, we are concerned that they will naturally develop packages as an adjunct to current activities. ACB believes that a final rule must be explicit about the lack of authority of the GSEs to be packagers.

Financial Literacy is an Important Element of Mortgage Reform

One of ACB's five priority policy issues for 2002 is financial literacy. We strongly believe that consumers who know and understand what they are shopping for are the best homebuyers. Unfortunately, many consumers do not understand what is involved in the home purchase process. We believe that education must begin before the consumer makes an application. We are concerned that the role of housing counselors will be diminished as a result of this proposal. If a borrower requests information from a lender, the lender may feel that he/she is precluded from giving information about counseling that the consumer may need to qualify for a mortgage. As mentioned above, we believe that the booklet is the place to include much explanatory information about the mortgage process. Even so, the booklet should be regarded as a compliment to other financial literacy initiatives.

Responses To HUD Questions For Commenters

We address below the questions presented by HUD with respect to the revised GFE, proposed Guaranteed Mortgage Package, and the disclosure of mortgage broker compensation. The questions are numbered as they are in the proposal.

The New Good Faith Estimate (GFE) Requirements (#1-10, #29-30)

We do not address each HUD question regarding the revised GFE requirements as proposed. As noted above, ACB believes that HUD should not adopt any changes to the GFE at this time. We have noted a number of changes that must be made to the proposed GFE before it can be adopted. We strongly urge that HUD revise that portion of the proposal and reissue it for comment. From a training, compliance and systems changes standpoint, the overall proposal is of such a magnitude that it must be considered and implemented in stages. GFE changes should be put off until the HUD and the industry have implemented and tested the Guaranteed Mortgage Package.

Guaranteed Mortgage Package Agreements

11. Is a safe harbor along the lines proposed in Section III.C.(1) of this rule necessary to allow lump sum packages of settlement services to become available to borrowers? Would the proposed clarification by HUD that discounts may be arranged, if passed on to borrowers and not marked up, suffice to make packages available to borrowers? Would a rule change to approve volume discounts and/or mark-ups when a package is involved suffice? Would it suffice to trim the disclosure requirements for packaging and offer the option of providing a streamlined GFE to those who packaged?

ACB believes that a Section 8 safe harbor exemption is appropriate to allow packagers to negotiate freely with settlement service providers for lower costs, which are then passed onto the borrower. The Guaranteed Mortgage Package not only provides upfront information about certain closing costs, it also provides the borrower with a measure of certainty about the cost of the loan, which potentially makes comparison-shopping easier and more fruitful. A narrow exemption allowing for volume discounts and/or mark-ups may unnecessarily constrain the range of possible lender/vendor negotiated arrangements. Without a safe harbor, packagers will not have the incentive to enter into such arrangements for fear of unintentionally violating Section 8 and being subject to increased risk of litigation.

While we generally support this part of the proposal, we reiterate that several important changes must be made to ensure the viability of the option.

12. As proposed in Section III.C.(6) is the scope of the safe harbor appropriately bounded in applying to all packagers and participants in packages? The safe harbor also currently does not apply to referrals to the package. Should there also be a bar against part time employees of other providers working for the package to steer business? How should the safe harbor apply to affiliated business arrangements to protect borrowers from steering?

ACB believes that the safe harbor should flow to the affiliated business arrangements. The goal of the Guaranteed Mortgage Package option is that consumers will be told a price for the package. It is not important how the lender or packager reaches the price within the package. There may be any number of ways for the package to be put together. One option is using the services of an affiliate. Another way may be for a third party to coordinate, subcontract, or otherwise negotiate and arrange a Guaranteed Mortgage Package.

13. As proposed in Section III.C.(5), to qualify for the safe harbor, the packager must include an interest rate guarantee with a means of assuring that when the rate floats, it reflects changes in the cost of funds not an increase in originator compensation. For this purpose, the rule suggests tying the rate to an observable index or other appropriate means. What other means could assure borrowers that the rate of a lender was not simply being increased to increase origination profits? For example, would a lender's commitment to constantly make rates public on a web site be a useful control? If an index is the best approach, how should it be set? If an index approach is approved, should each lender be allowed to pick its own observable index?

The requirement that the interest rate must float according to an observable and verifiable index is highly problematic and does not take into account numerous legitimate pricing concerns. As noted above, finding a loan product that meets the borrowers' needs may require that the consumer be turned down for the loan alternative for which they first applied. Interest rate is one factor in the loan options. Earlier industry discussions with HUD regarding RESPA reform focused on settlement services and did not include an interest rate guarantee. If HUD insists on making the lender commit to an interest rate spread, the industry needs more time to work with HUD on a reasonable solution.

Many lenders, particularly those that hold loans in portfolio, have costs of funds that vary from established national interest rate indices. The rates at which loans are offered are significantly affected by the costs of funds. Therefore, should an index approach be adopted, it is essential that lenders be permitted to establish their own observable indices.

In addition, HUD must work with the federal banking agencies to ensure that supervisory and accounting concerns have been addressed.

14. As discussed in the preamble to the rule in Section III.C.(5), if an observable index or other appropriate means of protecting borrowers from increases in lender compensation when the borrower floats in a guaranteed packaging approach is not practical, should HUD provide a packaging safe harbor only for mortgage brokers? Such a mortgage broker safe harbor would require disclosing the lender credit to the borrower in broker guaranteed packages. The theory for the safe harbor would be that any amounts in indirect fees could be credited to borrowers taking away any incentive for an increase in rates to increase compensation. Should this be offered in any event?

No, the safe harbor exemption should not be available only for mortgage brokers.

15. As proposed in Section III.C.(6), under the rule, mortgages with total fees or a rate covered by the Home Ownership and Equity Protection Act (HOEPA) would be subject to the new GFE disclosure requirements; however, HOEPA loans would not qualify for the guaranteed package safe harbor. Is this exclusion appropriate considering, on the one hand, that packaging promises borrowers a simpler way to shop and make transactions more transparent? On the other hand, the safe harbor could be provided for a loan that has very high rate and/or fees and may be predatory. The proposal also says that during *the rulemaking other limitations may be established to exclude high cost and/or loans with predatory features from the packaging provisions. HUD invites comments on whether HOEPA loans, any other loans, or features of loans should be included or excluded from the safe harbor and why.*

The exclusion of HOEPA loans from the safe harbor exemption is inappropriate. ACB believes that the safe harbor exemption should apply to HOEPA loans because in many cases HOEPA borrowers are those most in need of a Guaranteed Mortgage Package option. This also would steer the very customers that need clear information away from regulated lenders. Guaranteed settlement cost offers will help HOEPA borrowers focus on obtaining the best loan price available to them in the marketplace. Moreover, the most effective measure against abusive lending practices is to provide consumers with clear, upfront relevant settlement cost information that enables them to comparison shop mortgage loans.

16. As proposed in Section III.C.(3), the GMPA provides that the offer must be open to the borrower for at least 30 days from when the document is delivered or mailed to the borrower. Is this an appropriate minimum time period to ensure that the borrower has an adequate opportunity to shop?

The Guaranteed Mortgage Package offer should be open for a period of five business days. We believe that one week is ample time for a consumer to shop the guaranteed package cost. After borrowers sign a contract to purchase a property, they want to lock into a Guaranteed Mortgage Package quickly. Most contracts for a home purchase require that an application for credit be made with in five days. Also, borrowers who are refinancing existing mortgages usually want to close as quickly as possible. Once the borrower accepts the Guaranteed Mortgage Package, the packager should be able to require that settlement occur by a certain date for the offer to remain effective.

17. As proposed in Section III.C.(4), the rule currently provides that the Guaranteed Mortgage Package agreement must indicate that certain reports such as the appraisal, credit report, and pest inspection are available to the borrower upon the borrower's request. Also, packagers may decide to forego such reports or services (i.e. lender's title insurance) and must inform the borrower that such reports or services are not anticipated to be included in the package price. Are these adequate protections for the borrower? HUD is aware that other laws such as Regulation B (ECOA) provide certain rights to borrowers with respect to obtaining some of these reports. In order to qualify for the safe harbor HUD has created additional reporting requirements. Are these additional reporting requirements appropriate?

It is important that HUD work with the Federal Reserve to ensure compliance with ECOA and other consumer protections laws that require delivery of the documents. HUD can adhere to the packaging concept by requiring that the packager inform consumers that they may inquire whether the packager has obtained these reports and to leave it to the lender's discretion whether to provide them to the consumer.

18. Should additional consumer protections be established for packaging? For example, should additional qualifications be established for "packagers" to ensure that borrowers are protected against non-performance including the unavailability of a mortgage that could result in a borrower "losing" a house? For example, should there be a requirement that a packager must have sufficient financial resources to credibly back the guarantee? Is it necessary to require a lender signature on the GMPA to ensure that the borrower receives the loan at the time of settlement? How can the borrower's interests be protected without unduly burdening the process or unduly limiting the universe of packagers?

We do not believe that it is necessary to codify additional consumer protections for packaging that is performed by insured depository institutions, which are subject to regular supervision and examination. It may be worthwhile for HUD to develop additional consumer protections or financial strength requirements for packagers that are not depositories or are not lenders.

19. Consistent with the HUD-Fed Report, the rule proposes that certain charges, such as hazard insurance and reserves, are outside the package as other or optional costs. Is this the right approach or should these charges be disclosed as the minimum amounts required by the lender and required to be inside the package? Would the latter better serve the objective of establishing a single figure for the borrower to shop with?

While we strongly agree with HUD's approach to include as many services as possible in the package, escrow reserves for taxes and insurance should remain outside of the package. Borrowers do not shop based on these amounts and RESPA's escrow rules assure that permissible escrow cushions are not exceeded.

20. The rule proposes in Section III.C.(3), that under Guaranteed Mortgage Packaging, the HUD-1 will list the settlement services in the package but not the specific charges for each service. Certain third party charges are excluded from the calculation of the finance charge and the APR under TILA and HOEPA. Commenters are invited to express their views on whether the approach in the rule satisfies or whether alternative approaches to cost disclosures should be established to ensure consumers' rights under TILA and HOEPA are protected while facilitating packaging. More broadly, commenters are invited to provide their views on means of better coordinating RESPA and TILA disclosures.

We believe that the information contained in the initial TILA disclosure should not be duplicated in the Guaranteed Mortgage Package. However, we suggest that the disclosures be coordinated and perhaps consolidated so that consumers can make choices based on as few documents as possible. Duplicative disclosures would be costly to lenders and confusing to consumers. However, we recommend that HUD work with the Federal Reserve to ensure that the TILA disclosures do not conflict with those given as part of the package.

21. Commenters are asked to provide their views on how the rules should treat mortgage insurance? The rule proposes in Section III.C.(3), that the guaranteed package would include any mortgage insurance premiums in the APR and up-front costs of mortgage insurance in the guaranteed package. "Other Required Costs" would include reserves for mortgage insurance premiums. However, because the packager will not have an appraisal at the time the GMPA is provided, the packager may not have firm information to provide a definite figure. Another possibility is to exclude mortgage insurance from the package but notify the borrower that mortgage insurance may be an "Other Required Costs" and present the borrower an estimate subject to a tolerance, if mortgage insurance is necessary. This approach would exclude a major charge from the package. HUD recognizes that there are state laws that prohibit rebates or any splitting of commissions for mortgage insurance. How, if at all, should this impact the decision to include mortgage insurance in packages of settlement services?

ACB understands that ascertaining the cost of mortgage insurance at the time of application may be difficult. Nevertheless, mortgage insurance premiums can constitute a large cost to the borrower at closing and, therefore, should be disclosed to the extent possible. A lender should quote the amount of mortgage insurance premium that it would require based on the representations in the borrower's application, and if the circumstances change, the mortgage insurance amount may change as well.

22. To what extent, if any, do inconsistencies currently exist, or would they exist upon promulgation of the proposed rule between State laws and RESPA? Specifically, what types of State laws result in such inconsistencies and merit preemption? What, if any, provisions of the proposal should be revised to facilitate any necessary preemption?

Many inconsistencies exist between the proposal and state laws relating to disclosures, state RESPA and TILA laws, fee and interest rate restrictions and tie-in restrictions, to name a few. We recommend that HUD do a review of these state laws and work with the appropriate state supervisors to resolve any conflicts. We also suggest that HUD review these state laws to determine which can be preempted as being less favorable to consumers. HUD may determine that it is necessary to seek Congressional action to grant a broader preemption.

23. The rule proposes that the GFE and the GMPA be given subject to appraisal and underwriting. How should the final rule address the matter of loan rejection or threatened rejection as a means of allowing the originator to change the GFE or GMPA to simply earn a higher profit?

If the borrower accepts a Guaranteed Mortgage Package offer and upon full underwriting the packager determines that the applicant does not qualify at the preliminary rate offered in the Guaranteed Mortgage Package, the lender must either counter offer or issue a notice of adverse action. If a counter offer were given, a new Guaranteed Mortgage Package offer would be given, re-initiating the shopping process.

ACB believes that any final rule must address the issue of loan rejection and counteroffer. Because both the GFE and the Guaranteed Mortgage Package costs are being given based on information the consumer has supplied without full underwriting or appraisal being done, it is likely that changes will have to be made to the disclosures. Sometimes this is because there is a loan product that is better suited for the consumer, or it is because the appraisal does not show that the property is worth what the consumer believes it to be worth. ECOA requires a notice and process be used if the borrower is rejected. We understand that terms may change several times during the course of a transaction. This is a situation that must be addressed in any final rule.

24. To what extent, if any, should direct loan programs such as those provided by the Rural Housing Service of the Department of Agriculture be treated differently under the new regulatory requirements proposed by this rule?

The loans made pursuant to the loan programs of the Rural Housing Service should be treated the same way that all other first mortgage loans are treated. We do not believe that they should be excluded from these requirements.

25. As proposed, the GFE and GMPA currently contain sections for loan originators and packagers to indicate the specific loan terms for adjustable rate mortgages, prepayment penalties, and balloon payments. Are these appropriate loan terms to include on these forms, and what, if any, other mortgage terms or conditions should be listed on the forms?

These loan terms are duplicative of information already contained in the TILA disclosures and may increase costs to lenders and confuse consumers.

26. What are the arguments for or against limiting the proposed rule to purchase money, first and second lien, and refinancing loans as opposed to offering it to home equity, reverse mortgage and other transactions? Should there be any additional requirements for so-called B, C, and D loans?

We believe that the Guaranteed Mortgage Package should apply to home equity lines of credit to allow consumers to better compare prices and shop for theses types of loans.

27. As proposed, the Guaranteed Mortgage Package includes one fee for settlement services required to complete a mortgage loan. The fee for the package will include loan origination fees, typically referred to as "points." As points are generally deductible under IRS rules, comments are invited as to how to determine which portion of the package prices should be deemed to constitute points.

Points need to be identified for both the borrower and the lender. Without the itemization contained in the existing GFE, the identification process will be greatly impeded. It is important to consider that a lender, auditor, customer, or examiner must be able to reconcile what appears on the Guaranteed Mortgage Package and what is reported to the Internal Revenue Service and taken as a deduction by the borrower. This is an example of an issue that must be resolved for the Guaranteed Mortgage Package to succeed.

28. To what extent do the proposed changes to the definition of application in Section III.B.(2) a., and requirements for delivery of the GFE impact other federal disclosure requirements, such as those mandated by the Truth in Lending Act? How can the disclosure objectives of the proposed rule be harmonized with such other disclosure requirements?

ACB believes that it is necessary to coordinate any disclosures with those required by TILA, HMDA, ECOA and other consumer protection statutes. An alternative is that "application" as defined in the proposal, be treated as an application for purposes of both Regulations X and Z, but should be treated as a "pre-qualification" for purposes of Regulations B and C. Treating a submission as an application for Regulation X and Regulation Z purposes simply assures that the applicant receives the disclosures necessary to shop for the best mortgage loan. However, creditors should not be forced to treat every submission for a Guaranteed Mortgage Package offer as an application for Regulation B and C purposes because to do so will create severe customer relations problems and skewed HMDA reporting.

Conclusion

ACB supports mortgage reform and believes that HUD's proposed RESPA changes are a good initial attempt. In order for consumers to benefit from RESPA reform, the rules have to be realistic and workable in the marketplace. Toward this end, we urge HUD to separate the implementation of the Guaranteed Mortgage Package from the revised good faith estimate. The Guaranteed Mortgage Package, with revisions, should take priority and be tested in the market as soon as practicable. Revisions to the good faith estimate should be postponed and reexamined after the Guaranteed Mortgage Package has been tested.

In order for a final rule to be implemented effectively, concerns and conflicts with other federal regulators and banking agencies must be reconciled. Similarly, HUD must address the existence of state laws that frustrate the underlying purpose of the packaging concept. Mortgage broker fee disclosure is an integral part of making mortgage fees comprehensible to consumers and should be implemented in the revised rule.

ACB encourages HUD to prohibit secondary market housing GSEs from packaging and we encourage HUD to apply the safe harbor exemption to HOEPA loans. Finally, we believe that revisions to the settlement booklet and other documents can be better accomplished when the importance of financial literacy is not ignored.

ACB appreciates the opportunity to comment on this very important matter. We stand ready to work with HUD to complete the RESPA reform process in a way that is efficient and feasible. Please do not hesitate to contact the undersigned at (202) 857-3121 or cbahin@acbankers.org or Janet Frank at (202) 857-3129 or jfrank@acbankers.org.

Sincerely,

Charlotte M. Bal

Charlotte M. Bahin
Directors of Regulatory Affairs, Senior Regulatory Counsel

December 27, 2001

Honorable Mel Martinez
Secretary
US Department of Housing and Urban Development
451 7^{th} St., SW
Washington, DC 20410

Dear Secretary Martinez:

The undersigned lending organizations represent every segment of the housing finance system in America, including national and regional lenders, large and small institutions, wholesale and retail lenders, mortgage conduits, and service providers. On behalf of our collective memberships, we want to thank you for the recent clarifications concerning the legality of lender payments of yield spread premiums to mortgage brokers under the Real Estate Settlement Procedures Act (RESPA). As we have expressed on previous occasions, HUD's recent pronouncements are essential to providing the necessary legal certainty to preserving yield spread premium payments as an option for the financing of closing costs, thereby making homeownership available to more Americans.

Our memberships continue to be supportive of your ongoing initiative, as set forth in the recent Statement of Policy 2001-1, to ensure that consumers receive full and meaningful disclosures in the mortgage process, and we collectively reiterate our full endorsement of your commitment to clarify and improve the home-buying process. In this spirit, we are submitting a model disclosure entitled Mortgage Broker Fee Agreement ("Agreement") that we believe meets all of the disclosure features that HUD identifies in Policy Statement 2001-1.

The attached form was designed by a diverse working group of large and small mortgage lenders, legal experts, and practitioners and we believe it sets forth the most feasible prototype for a useful consumer disclosure. The attached Agreement has been approved by all signatory lender associations, and was fashioned to expressly accommodate all of HUD's "best practices" factors while incorporating useful features of the MBA/NAMB Model Form and other state disclosures that are currently in use. We believe that the attached model meets HUD's expectations and provides a balanced approach to fully disclosing the compensation paid to mortgage brokers.

Honorable Mel Martinez
Page 2

We also wish to take this opportunity to communicate our concerns over HUD's apparent call for an additional disclosure relating to amounts received by lenders for the sale of loans in the secondary market. The matter of secondary market fee disclosures has been thoroughly debated and considered in previous HUD proposed rulemaking proceedings and in the context of regulatory negotiations; in every instance, the sound legal principle and interpretation that secondary market payments are exempt from RESPA has remained intact. We make clear that our collective membership opposes any shift or dilution of this longstanding exemption. We would welcome the opportunity to discuss this issue further with you or your staff.

On the whole, our organizations continue to believe that comprehensive mortgage reform is the most effective way to resolve the continuing regulatory difficulties under RESPA while ensuring that consumers are afforded with the information necessary to adequately shop for mortgage credit. We also believe that significant portions of these mortgage reform measures can be achieved immediately, under HUD's existing regulatory authority. We affirm our continuing commitment to working with the Department on these regulatory improvement efforts and urge that you meet with us to discuss our groups' agreed approach in detail.

Once again, our organizations commend you and the members of your staff who contributed to this effort. We look forward to continuing our partnership with HUD throughout this rulemaking process and again thank you for restoring confidence in our nation's robust housing and mortgage finance market.

Sincerely,

America's Community Bankers
American Bankers Association
Consumer Mortgage Coalition
Mortgage Bankers Association of America

Mortgage Broker Fee Agreement

In the following: "I" or "me" = applicant; "You" = mortgage broker

Mortgage Broker Service. You are duly authorized and prepared to assist me in arranging mortgage financing for my home, and you agree to provide such assistance, as set forth below.

Amount of Broker Compensation. I understand that, as compensation for the goods, services and facilities you provide, your total mortgage broker compensation from all sources will not exceed:

[$______________]

and / or [*specify which*]

[______________ point(s)] (one point equals 1 percent of the original principal balance of the actual mortgage loan obtained).

Method of Broker Compensation Payment. I understand that I may have a choice as to how your compensation is paid. Depending on such factors as my financial circumstances, whether I qualify for a loan and/or whether a loan program is available:

- I may pay your compensation for the services you provide out of my pocket directly.
- If I want to lower the amount I compensate you out of my pocket directly:

  → I may have the lender pay some or all of your compensation, in which case the lender will charge me a higher interest rate which could result in higher monthly payments; and/or

  → I may use the proceeds of the loan to pay some or all of your compensation, in which case I will be obligated to repay that amount with interest over the term of the loan.

I understand that I should discuss with you in further detail the specific options available to me to pay for your compensation, including the impact of each such option on the amount of cash I must bring to the closing, my interest rate, loan amount and monthly payments.

Nature of the Relationship. [Choose appropriate text][standard][I understand that in connection with this Agreement, you are not acting as my agent. You are also not acting as the lender's agent. Although you seek to assist me in meeting my financial needs, you may not make available the products of all lenders or investors in the market or the lowest prices or best terms available in the market.]

[California/FHA][I understand that in connection with this Agreement and any mortgage loan you arrange for me, you are acting as my agent. You are not acting as the lender's agent. Although you seek to assist me in meeting my financial needs, you do not distribute the products of all lenders or investors in the market and cannot guarantee the lowest price or best terms available in the market.]

[lender's agent] In assisting to arrange financing for my home, I understand that you are not my agent and that you are acting as the agent of the lender.]

Termination. This Agreement will continue until one of the following events occurs:

- I fail to receive loan approval;
- My loan closes;
- I terminate this Agreement;
- You and I enter into a new Mortgage Broker Fee Agreement; or
- ____________ days expire from the date of this Agreement without any of the foregoing occurring.

Mortgage Broker Fee and Disclosure Acknowledgement

By signing below, I/we understand and agree to the terms of this Agreement. The contractual obligation to comply with this Agreement rests solely with the mortgage broker and the applicants signing below. No other entity shall be liable for any misrepresentation or non-performance of the mortgage broker's obligations under this Agreement, or the mortgage broker's collection of compensation in excess of the maximum compensation amount stated herein.

Signing this Agreement does not obligate me to obtain a mortgage loan through you , nor does it prevent me from shopping for mortgage loans with any other mortgage broker or lender. This Agreement does not constitute a loan commitment or otherwise indicate mortgage loan approval.

I acknowledge that you and any lender that makes a loan to me is relying upon this Agreement and upon my statement that I actually understand your role in the transaction and how you will be paid.

* * Applicant____________________ Date________________

* * Applicant____________________ Date________________

____
Mortgage Broker's Signature
Mortgage Broker's License No. (where applicable) ____________________

UNIFORM MORTGAGE COSTS DISCLOSURE

#3

Please take this disclosure with you to settlement to compare costs.

We agree to perform or provide services, goods or facilities to assist you in the origination of a mortgage loan. The services, ~~goods~~ or facilities may be performed or provided for your direct benefit, or some of them may benefit you only indirectly, in that they are performed on behalf of third parties (e.g., wholesale lenders or secondary market investors) but are necessary to the objective of obtaining the mortgage loan you desire. While we seek to assist you in meeting your financial needs, we cannot guarantee the lowest price or best terms available in the market. We, as with all originators, may not offer all the products that are available in the marketplace.

The information provided below reflects our disclosure of the charges you will incur at the settlement of your loan. The "Origination Costs" are fees charged by your originator or an investor for providing a mortgage loan. "Settlement Costs" are fees for third party services that are required for the mortgage loan to close. These "Total Costs" are itemized for you in the grid below.

The following disclosure is valid for _____ days (7 days or greater) from the date this form is delivered to and signed by the borrower. This disclosure is dependent upon the borrower qualifying for this mortgage based on their credit rating, appraisal, and other appropriate criteria.

Summary of Loan Terms:
Property Address: ______________________________
This loan will be a _____ purchase ________refinance. This loan will be a ______ first mortgage _____second mortgage.
Loan Program: ______________________________Loan Term: ____________ Mortgage Loan Amount: ______________________
(See appropriate disclosure form)

%

Interest Rate ______ Initials

This is the interest rate for [today] for the loan you have selected. We will lock this rate for you for the following time period of _____ days. This interest rate lock will expire _______. I understand to obtain this interest rate loan, I may be required to pay a lock fee which is NOT INCLUDED in the costs disclosed on this form. If you choose not to lock your interest rate today, your interest rate may increase or decrease before settlement without notification.

_______**I want to lock my interest rate.** ________________ ________________
By signing above, you have agreed that this is the interest rate you will pay for this loan provided you qualify, regardless of market conditions. For this interest rate lock, you agree to pay $__________.

______ **I choose not to lock my interest rate. I understand that my interest rate may increase or decrease before settlement without prior notification.** ________________ ________________

$

Origination Costs ______ Initials

This is the total amount of costs being charged as origination costs. These costs are itemized below. These costs will not increase unless you are not eligible for this loan program, your property changes or does not qualify, you choose a different loan program, you choose a different pricing option, or your loan amount changes. This figure does not include any settlement costs that are paid to a third party.

$

Settlement Costs ______ Initials

This is the total amount of costs you will incur for the settlement of this loan. These costs are itemized below. As these costs are beyond the control of the originator, they are not guaranteed. However, if these fees change from initial disclosure, the originator is required to redisclose to you at a minimum of fifteen (15) days prior to settlement. Upon final disclosure, this amount cannot increase beyond 10% of the amount of the total amount of fees at settlement. You may waive the 15-day redisclosure requirement under certain conditions.

This figure does not include the following four costs: any escrows set up for taxes, any escrows set up for homeowners insurance, any escrows set up for mortgage insurance, and any per diem interest. Please see page 2 of this disclosure for an estimation of your hazard insurance, mortgage insurance, taxes, escrow amounts, and per diem interest.

$

Monthly Payment Initials

This is your monthly payment based on the above loan amount and the above interest rate. This payment **DOES** include the following:
________ Principal.
________ Interest.
________ Hazard insurance.
________ Real estate taxes.
________ Mortgage insurance.

After reading through the above information, please initial to the right of each box to show your acknowledgement and acceptance of the above data. Also, you need to indicate your preference by signing either the float or lock option in the "Interest Rate" section.

These estimates are provided pursuant to the Real Estate Settlement Procedures Act of 1974, as amended (RESPA). Additional information can be found in the HUD Special Information Booklet, which is to be provided to you by your mortgage broker or lender, if your application is to purchase residential real property and the lender will take a first lien on the property. The undersigned acknowledges receipt of the booklet "Settlement Costs", and if applicable the Consumer Handbook on ARM mortgages. The undersigned also acknowledges that I (we) have read both pages of this disclosure and that I (we) fully understand its terms. Further, by signing below, the undersigned authorize the originator to ______ order an appraisal, a credit report and continue the origination process___ draw documents in order to proceed to settlement.

Borrower Date Co-Borrower Date

Itemization of Total Costs

Origination Costs		Settlement Costs	
801 Loan Origination Fee		803 Appraisal Fee	
802 Loan Discount		804 Credit Report	
808 Mortgage Broker Fee		805 Lender's Inspection	
810 Processing Fee		806 Flood Zone Certification Fee	
811 Underwriting Fee		809 Tax Related Service Fee	
812 Wire Transfer Fee		1101 Closing or Escrow Fee	
		1105 Document Preparation Fee	
		1106 Notary Fees	
		1107 Attorney Fees	
		1108 Title Insurance	
		1201 Recording Fees	
		1202 City/County Tax/Stamps	
		1203 State Tax/Stamps	
		1302 Pest Inspection	
		1303 Courier Fee	

DISCLOSURE FORM

Additional Costs

Certain costs are not included in the above estimates as they are based upon personal choice on your part or are dependent upon when closing will be held. These amounts are estimated below based upon a closing date of ___________:

Per Diem Interest ___ days at $______ per day = ______________
Hazard Insurance for ___ months ______________ Amount to be Escrowed Each Month _______
Taxes for ____months ______________ Amount to be Escrowed Each Month _______
Mortgage Insurance for ___months ______________ Amount to be Escrowed Each Month _______

The total estimated amount of your monthly payment, based upon your loan program and amounts to be escrowed, is ________.

Interest Rate and Settlement Costs Options

1. Cash Payment at Settlement: You may pay all or part of your required settlement costs at settlement using your available funds.
2. Borrowing Additional Funds to Pay Settlement Costs: You may be able to pay all or part of your settlement costs by borrowing the needed funds as part of your mortgage loan principal. If you choose this option, your monthly payments will increase. This may not be available on a purchase-money loan.
3. Pay Settlement Costs Through a Higher Interest Rate: You may be able to lower your settlement costs in exchange for paying a higher interest rate on your mortgage loan. This higher interest rate will increase your monthly payments.
4. You May Lower Your Interest Rate: You may be able to lower the interest rate on your loan by paying additional funds at closing, commonly referred to as "discount points." The reduced interest rate will lower your monthly payments.

The following table provides a generic example of how higher and lower interest rates affect your loan and loan payments.

	GFE Terms You Selected	Higher Interest Rate	Lower Interest Rate
New Loan Balance	$100,000	$100,000	$100,000
Interest Rate	7.00%	7.25%	6.75%
Monthly Principal & Interest & PMI (if required)	$700.30	$717.18	$683.60
Change in Cash to Close from GFE Terms You Selected		$1,000 less	$1,000 more
Change in Monthly P&I from GFE Terms You Selected		$16.88 more	$16.70 less

$

Initials

Compensation For Goods, Facilities And Services For Your Loan

An originator may be compensated by an investor for goods, facilities or services provided to you or to the investor. This will result in a higher interest rate for this loan. If you would rather pay less cash up front, you may be able to pay some or all of the originator's compensation indirectly through a higher interest rate. If you would rather have a lower interest rate, you may pay higher up-front points and fees. This amount will not exceed the amount disclosed to the left of this description.

If the originator is acting as a lender in this transaction, the originator may receive additional compensation when it sells the loan for the value of the servicing rights or the value of the interest rate or a combination of both. This amount is not required to be disclosed.

ADDITIONAL LOAN TERMS

- ☐ This mortgage IS subject to a prepayment penalty.
- ☐ This mortgage IS NOT subject to a prepayment penalty.
- ☐ This mortgage HAS a balloon payment of ________, which will be due at the conclusion of the loan term. We may or may not refinance this mortgage.
- ☐ This mortgage DOES NOT HAVE a balloon payment.
- ☐ This mortgage IS assumable.
- ☐ This mortgage IS NOT assumable.

Adjustable Rate Mortgage (ARM) Loans

___This is an Adjustable Rate Mortgage (ARM) Loan. Your interest rate may increase or decrease depending on the market. THAT MEANS THAT YOUR MONTHLY PAYMENT MAY INCREASE OR DECREASE. Please refer to the ______________________loan program disclosure provided to you.

Details of Transaction

a. Purchase Price	
b. Refinance (debts to be paid off)	
c. Estimated Prepaid items	
d. Estimated Closing Costs	
e. PMI, MIP, Funding Fee	
Total costs a-e	
- Subordinate Financing	
- Costs paid by seller	
- Other credits	
- Loan amount	
Cash from/to borrower	

You will need to bring approximately $___________ with you to settlement. This amount may change. This form must be signed and returned within seven (7) days of receipt

NAIC
making progress . . . together

NATIONAL ASSOCIATION OF INSURANCE COMMISSIONERS

EXECUTIVE HEADQUARTERS

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WORLD WIDE WEB

www.naic.org

February 13, 2003

Rules Docket Clerk
Office of General Counsel
Room 10276
United States Department of Housing and
Urban Development
451 Seventh Street, S.W.
Washington, D.C. 20410-0500

Re: *Proposed Rule "Real Estate Settlement Procedures Act (RESPA); Simplifying and Improving the Process of Obtaining Mortgages To Reduce Settlement Costs to Consumers" (24 CFR 3500)*
Docket No. FR-4727-P-01

Dear Sir/Madam:

Please accept the following comment from the National Association of Insurance Commissioners ("NAIC") on the effects that the proposed rule referenced above will have on the state regulation of title insurers. Although the comment due date was October 28, 2002, we hope that you will still accept our comment for review. The comment will address Question 22 (Should Inconsistent State Laws Be Preempted) as listed in the "Questions for Commenters" section of the proposal which reads in full as follows: To what extent, if any, do inconsistencies currently exist, or would they exist upon promulgation of the proposed rule between State laws and RESPA? Specifically, what types of State laws result in such inconsistencies and merit preemption? What, if any, provisions of the proposal should be revised to facilitate any necessary preemption?

The NAIC is a nonprofit corporation, founded in 1871, whose membership consists of the chief insurance regulators from the 50 states, the District of Columbia and the four U.S. territories. It is a 501(c)(3) charitable, educational institution organized to assist state regulators, individually and collectively, in serving the public interest and achieving the fundamental insurance regulatory goals in a responsive, efficient and cost-effective manner. The NAIC provides a forum for the development of uniform policy when uniformity is appropriate. A state regulator's primary responsibility is to protect the interests of insurance consumers, and the NAIC helps regulators fulfill that obligation. The NAIC's primary instruments of public policy are model laws, regulations and guidelines, which are developed at NAIC meetings for members' use. The states may either adopt the models intact or modify them to meet their specific needs and conditions.

This comment will first discuss the NAIC's concern that the proposed rule of the Department of Housing and Urban Development (HUD) relating to the "Guaranteed Mortgage Package" (GMP) may, if adopted, lead the proponents of the packaging concept to encourage HUD to use Section 18 of RESPA to pre-empt state rate filings and standards laws for title insurance and the impact that this will have on the title insurance industry and consumers. Secondly, it will address the NAIC's concern that the proposed HUD rule may, if adopted, lead the proponents of the packaging concept to encourage HUD to use Section 18 of RESPA to pre-empt state insurance laws prohibiting rebates (or kickbacks) and fee-splitting and the impact that this will have on the title insurance industry and consumers. Finally, it will address the fact that HUD lacks the statutory authority to pre-empt these state insurance laws.

I. The NAIC and State insurance regulators are concerned that the proposed rule relating to the GMP may, if adopted, lead the proponents of the packaging concept to encourage HUD to use Section 18 of RESPA to pre-empt state rate filings and standards laws for title insurance.

The NAIC Title Insurers Model Act, section 19 provides that all title insurance companies are required to get approved and pre-file with the commissioner their schedule of fees and rates in accordance with applicable statutes and regulations governing rate filings, and may not charge any fee for any policy or contract of title insurance except in accordance with the filed rates.[1] State rate filing laws for title insurance companies have been adopted by most of the states.

In agreement with many of the comment letters that you have already received, the NAIC and State insurance regulators are concerned that the components of the proposed rule relating to the GMP may, if adopted, lead the proponents of the packaging concept to encourage HUD to use Section 18 of RESPA to pre-empt this NAIC model act which regulates title insurance rate filing and oversight requirements and all state laws that have adopted this model act provision. Specifically, the concern of the NAIC and State insurance regulators is that HUD's proposed rules may enable mortgage providers or others who include title insurance in a guaranteed package of mortgage-related products and services to bypass the state laws which regulate title insurance rate filing and oversight requirements, thereby creating the potential for the utilization of title insurance rates that are inadequate or unfairly discriminatory.

The primary public policy objective underlying the laws requiring the filing of rates with, and their oversight by State insurance regulators is to ensure the ongoing financial solvency of insurers and to ensure that consumers get a good deal and are protected. State laws regulating rates which title insurance companies may charge are designed to provide the public with reasonable prices but which are sufficient to guard against the insolvency of insurers and enable them to provide the public with timely and effective services. The utilization of inadequate rates jeopardizes the financial solvency of the title insurance company. Title insurance (and mortgage

[1] Section 19 of the NAIC Title Insurers Model Act states in pertinent part:

A. No title insurer may charge any rates regulated by the state after the effective date of this Act, except in accordance with the premium rate schedule and manual filed with and approved by the commissioner in accordance with applicable statutes and regulations governing rate filings. The commissioner may provide by regulation for interim use of premium rate schedules in effect prior to the effective date of this Act.

guaranty insurance) differs from other lines of insurance in that the basic goal of each is risk elimination. Title insurance ensures that the policyholder has title to the property on the subject real estate as of the date of policy issuance, subject to exceptions and exclusions in the policy. When issued, a title policy has a one-time nonrefundable premium and reserves are established by the title insurance company. The reason for this is that the event which may cause the loss insured against has already occurred at the time of issuance, so the premium actually covers the past risk and not future risk. Title insurance rates are therefore risk based rather than market based. In proposing to combine settlement costs with interest rates in the GMP, HUD is combining two costs with entirely different levels of volatility and risks for lenders. HUD's proposed GMP rates are market based, which if used for title insurance rates will lead to insolvencies of title insurance companies. In the context of title insurance, were a valid claim to be made, the consequences of the title insurer's insolvency to the holder of a mortgage secured by, and to the owner of the affected property could be devastating.

We understand that HUD's primary objective in its proposed rule relating to the GMP is to reduce the consumers cost, however, in doing so, HUD seems to be looking solely at how to create the lowest price for the mortgage package. For the reasons stated above, title insurance which is a risk-based product is very different from all of the other services that are included in the mortgage package. Since title insurance is a risk-based product and its premiums are risk based, its rates should not be discounted, as HUD's proposed rule would permit. It would do consumers little good to purchase insurance policies of an insurer at a discount which, on a cumulative basis erode the insurer's revenue and capital as to ultimately endanger the insurer's ability to handle and pay claims under those policies. If any of the other service providers that are included in the mortgage package go out of business after the closing date, there would be no negative impact to the consumer. However, we stress that HUD needs to consider the devastating consequences that the insolvency of a title insurance company will have on consumers. As we stated above, the primary public policy objective underlying the state laws requiring the filing of rates with, and their oversight by state insurance regulators is to ensure the ongoing financial solvency of title insurers.

We find it important to point out to HUD at this time that mortgage guaranty insurance, an insurance paid for by the borrower for the benefit of the lending institution which covers the default of the borrower is also a risk based product and is not market based. The difference between title insurance and mortgage guaranty insurance is that title insurance covers past risks and mortgage guaranty insurance covers future risks. Therefore, mortgage guaranty insurance rates like title insurance rates should not be discounted, as HUD's proposed rule would permit.

II. The NAIC and State insurance regulators are concerned that the proposed rule relating to the GMP may, if adopted, lead the proponents of the packaging concept to encourage HUD to use Section 18 of RESPA to pre-empt state insurance laws prohibiting rebates (or kickbacks) and fee-splitting.

Pursuant to section 17 of the NAIC Title Insurers Model Act and section 5 of the NAIC Title Insurance Agent Model Act, rebates and fee splitting are prohibited.[2] Most states have laws modeled on these NAIC Model Acts and have incorporated these prohibitions into their statutes.

Under the proposed rule, to encourage the offering of discounts in prices by third-party settlement service providers, lenders who package and those providers offering services covered by the package would be given an exemption from RESPA §8's prohibition of referral fees and fee-splitting. The proposed exemption for lenders and the providers of services in the packaging from the anti-kickback (anti-rebate) and fee-splitting provisions of RESPA §8 (which prohibition has been in effect for approximately thirty years) will encourage payments to mortgage lenders that will conflict with the NAIC model laws and similar state laws. Under the GMP, agents will be able to split commissions and give rebates to clients. The State insurance regulators are concerned that HUD is moving in a direction opposite to that of State insurance regulators and legislatures by lifting these provisions of RESPA, especially when it is not achieving pro-consumer benefits. Under the proposed GMP, lenders or other packagers are not required to pass on discounts to the consumer but may profit from any discounts, kickbacks or rebates which settlement providers offer to the packager. RESPA's §8 has developed into an important corollary to the state insurance laws prohibiting rebates and fee-splitting. To remove this restriction can only lead in the direction of encouraging lenders to seek business arrangements which insurance regulators have through experience found to be destructive to the industry and in the end, consumers.

III. HUD lacks the statutory authority to pre-empt these state insurance laws.

These current state laws which are sought to be swept away by the proposed HUD rules are not inconsistent with RESPA and provide greater protection to consumers. The proposed HUD rules constitute an attempt to regulate disclosures and the pricing of loan costs and settlement services that is inconsistent with the RESPA regime created by Congress. The impact that the proposed HUD rules will have on the title insurance industry will be great as they will have a negative impact on the financial solvency of the title insurance companies.

Section 18 of RESPA, 12 U.S.C. 2616, states:

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[2] Section 17 of the NAIC Title Insurers Model Act states in pertinent part "A title insurer or other person shall not give or receive, directly or indirectly, any consideration for the referral of title insurance business or escrow or other service provided by a title insurer."

Section 5 of the NAIC Title Insurance Agents Model Act states in pertinent part "A title insurance agent or other person shall not provide or receive, directly or indirectly, any consideration for the referral of title insurance business or escrow or other service provided by a title insurance agent."

> This Act [RESPA] does not annual, alter, or affect, or exempt any person subject to the provisions of [RESPA] from complying with, the laws of any State with respect to settlement practices, except to the extent that those laws are inconsistent with any provision of [RESPA], and then only to the extent of the inconsistency. The Secretary is authorized to determine whether such inconsistencies exist. The Secretary may not determine that any State law is inconsistent with any provision of [RESPA] if the Secretary determines that such law gives greater protection to the consumer. (emphasis added). In making these determinations the Secretary shall consult with the appropriate Federal agencies.

Accordingly, the Secretary's ability to make preemption determinations under Section 18 of RESPA comes into play if a provision of State law is inconsistent with a provision of RESPA, as enacted by Congress. The State laws discussed are not inconsistent with RESPA §8 as enacted by Congress, or any other provision of RESPA. Additionally, the Secretary simply does not have such broad authority pursuant to §18 of RESPA to pre-empt State insurance laws designed to protect consumers from unsafe and unsound insurance practices. Furthermore, HUD has no legal authority to promulgate a rule pre-empting these State insurance laws as described in the proposed rule. Whether these State insurance laws should be pre-empted is an issue that should be resolved by Congress.

Congress has clearly expressed its intent that the States exercise jurisdiction in the regulation of insurance. The McCarran-Ferguson Act (15 U.S.C. 1011 et seq.) which was passed by Congress in 1945 provides that "the business of insurance, and every person engaged therein, shall be subject to the laws of the several States which relate to the regulation or taxation of such business." The Gramm-Leach Bliley Act ("GLBA" or the "Financial Services Modernization Act of 1999") has recently reaffirmed the McCarran-Ferguson Act. (GLBA Section 104(a)). To the extent that the proposed HUD rules violate the McCarran-Ferguson Act, the courts will strike it down.

The regulatory framework established by GLBA designates the States as the appropriate functional regulators of insurance products in the United States, including those provided by Federally-supervised banking and securities firms. This most recent Federal statutory affirmation of State insurance authority is wise because it recognizes the States successful record over the years in meeting the special consumer protection requirements of insurance products. In its passage of GLBA, Congress showed deference to State laws regulating the business of insurance in general, and specifically, the business of title insurance. There is no indication from Congress in its passage of GLBA that it intended to pre-empt these State insurance regulatory statutes. Congress directly confronted the question of preemption of insurance laws in its enactment of GLBA. Far from embracing broad preemption of State insurance laws, Congress explicitly preserved State insurance regulation with respect to insurance activities of depository institutions, activities of the kind contemplated by HUD's proposed rule.

IV. Recommendation to HUD

For the reasons stated above, since title insurance and mortgage guaranty insurance are risk based products rather than market based services and are therefore very different from all of the other services that are included in the mortgage package, the NAIC and State insurance regulators respectfully request HUD to exclude title insurance and mortgage guaranty insurance from the GMP.

In the alternative, in agreement with the New Jersey Department of Banking and Insurance (NJDBI), the NAIC and State insurance regulators would respectfully urge HUD to include text in the rule, or otherwise specifically provide that state insurance departments will retain the authority to review and approve the adequacy of any title insurance rates and related fees included in a guaranteed mortgage package offered pursuant to the proposed rule. Doing so will preserve the ability of the states to verify that such rates and fees are sufficient to ensure the ongoing financial solvency of the title insurance underwriter and are not excessive or unfairly discriminatory.

The NAIC and State insurance regulators do not want to be viewed as obstructing the financial modernization goals of GLBA. Recognizing the need for improved cooperation and communication with federal financial services regulators, particularly in the wake of the enactment of GLBA and the convergence of the financial services industry, the NAIC and the State insurance regulators look forward to working with HUD.

The NAIC and State insurance regulators appreciate your consideration of its concerns and would welcome the opportunity to schedule a meeting with representatives of HUD in order to discuss or clarify any of the issues discussed above, or to provide any additional information that HUD may require.

Respectfully submitted,

Mike Pickens
President, National Association of Insurance Commissioners

cc: The Honorable Mel Martinez, Secretary, Housing and Urban Development
The Honorable John C. Weicher, Assistant Secretary, Housing/Federal Housing Commissioner
Members of the Senate Banking Committee
Members of the House Financial Services Committee

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February 24, 2003

Chairman Robert Ney
Housing and Community Opportunity Subcommittee
House Committee on Financial Services
Rayburn House Office Building, Room B303
Washington, DC 20515

Dear Chairman Ney:

On behalf of the American Bankers Association (ABA), I would like to submit this letter and the attached comment letter to be added to the hearing record of February 25, 2003 regarding proposed changes to the Real Estate Settlement Procedures Act (RESPA). The ABA brings together all categories of banking institutions to best represent the interests of this rapidly changing industry. Its membership – which includes community, regional and money center banks and holding companies, as well as savings associations, trust companies and savings banks – makes ABA the largest banking trade association in the country.

Mr. Chairman, the ABA appreciates your and your subcommittee's interest in seeking to improve and simplify the process of obtaining mortgages. Homeownership is a central pillar in our nation's economic strength and every effort should be made to make the system more efficient. In reaching this goal, coordination among HUD, the Federal Reserve and other bank regulators, and industry participants is a must. Without it, the likelihood increases of inadvertent costs and the benefits of RESPA reform will be lost. One need only look to the number of comment letters filed with HUD on the pending proposal to see how important this issue is to all participants in the housing sales and financing sector. Because of its complexity and the need for a measured and careful approach, we believe that HUD should ***re-propose*** its rule after taking into account the comments that have been submitted. We are concerned that HUD will not take this additional, important step, and we urge Congress to encourage the agency to do so.

It is important in the discussion of RESPA reform to recognize that the participants in the mortgage finance industry are subject to different regulatory oversight. Banks are subject to intensive examination by their chartering and/or supervisory agencies and those agencies not only extensively examine banks for safety and soundness concerns but also oversee their compliance with numerous statutes and regulations such as RESPA and Regulation X. Banks undergo intensive scrutiny during this process. Many participants in the mortgage process that are not banks, their subsidiaries, or affiliates never receive such a thorough RESPA review. As it proceeds with a proposed rule, HUD should ensure that banks not endure additional regulatory burden because other participants in the mortgage process do not undergo such a thorough and frequent examination process.

Coordination is a must in this process, as there are other laws– especially the Truth in Lending Act (TILA) and its implementing regulation, Regulation Z – that govern aspects of the mortgage lending process. Importantly, the disclosure of mortgage loan terms is not the purview of RESPA or Regulation X. Congress assigned that role to TILA and the Federal Reserve Board. The proposed rule is contrary to the intent of both RESPA and TILA in this regard. Also, the proposed rule preempts Congress's decision that certain terms are important and should be segregated and highlighted, as delineated in TILA. For example, TILA is designed to "assure a meaningful disclosure of ***credit terms*** so that the consumer will be able to compare more readily the various credit terms available to him and avoid the uninformed use of credit." (Emphasis added.)

In contrast, RESPA's purpose, with regard to mortgage terms is to "effect certain changes in the settlement process for residential real estate that will result in more effective advance disclosure to home buyers and sellers of ***settlement*** costs. . . " (Emphasis added.)

Clearly, Congress intended TILA to govern loan term disclosure and RESPA to cover settlement costs. However, the proposed rule preempts this intention by mandating disclosure of certain loan terms, including those related to costs, prepayment penalties, balloon payments, and adjustable rate mortgages. The proposed rule includes these terms notwithstanding that TILA and Regulation Z specifically address them. Even more importantly, the proposed terms are in some cases inconsistent with Regulation Z.

Use of consistent definitions and elimination of redundant and often conflicting requirements is vital. Otherwise, the rule will only confuse consumers. Moreover, unnecessarily lengthening the form with redundant terms will also mean that consumers will be less likely to read the materials more carefully, if at all.

As it moves toward further consideration of the proposed regulation, HUD should ensure that there is sufficient lead-time before any final regulation is fully implemented. Lead-time is essential for many reasons: to ensure that the bank supervisory agencies are fully conversant in the final regulation and are trained to examine for its implementation; to enable banks to modify their mortgage origination policies and practices (including retraining of employees involved in the mortgage process as well as those overseeing compliance with RESPA and Regulation Z); to redesign their software programs to accommodate the changes incorporated in such a final regulation; and to restructure their marketing and compliance programs. This process is not a simple undertaking and would necessitate a significant expenditure of bank resources. A minimum of two years from the date of the final regulation should be instituted for full compliance.

Further details on ABA's position on these and other RESPA issues are provided in the attached letter, dated October 28, 2002, which was submitted to HUD.

The mortgage origination process is a complicated and important one, which in many instances, is the most significant transaction entered into by many borrowers. HUD is to be commended for its efforts thus far. ABA believes that real reform is possible, but that more steps are necessary to ensure that the current process is improved without unduly disrupting those elements of the system that are working. Mr. Chairman, the ABA appreciates your involvement with this issue and we pledge to work with your subcommittee and HUD to achieve our shared vision of an efficient and effective mortgage settlement process.

Sincerely,

Floyd E. Stoner

Floyd E. Stoner
Executive Director, Congressional Relations & Public Policy

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Attachment

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October 28, 2002

Rules Docket Clerk
Office of General Counsel
Department of Housing and Urban Development
Room 10276
451 Seventh Street, SW
Washington, DC 20410-0500

Re: Docket No. FR-4727-P-01; Department of Housing and Urban Development; Real Estate Settlement Procedures Act ("RESPA"); Simplifying and Improving the Process of Obtaining Mortgages to Reduce Settlement Costs to Consumers; 24 CFR Part 3500; 67 Federal Register 49133, July 29, 2002

Dear Sir or Madam:

The American Bankers Association ("ABA") appreciates the opportunity to comment on the Department of Housing and Urban Development's ("HUD") proposed rule designed to "simplify and improve the process of obtaining home mortgages and reduce settlement costs for consumers." In its attempt to meet this objective HUD significantly restructures the Good Faith Estimate ("GFE") and creates a new Guaranteed Mortgage Package ("GMP") arrangement. The American Bankers Association brings together all categories of banking institutions to best represent the interests of this rapidly changing industry. Its membership—which includes community, regional and money center banks and holding companies, as well as savings associations, trust companies and savings banks—makes ABA the largest banking trade association in the country.

The ABA applauds HUD's goals of improving and simplifying the process of obtaining mortgages to reduce settlement costs to consumers. ABA shares those goals and we want to continue to work with the Department in meeting them. Given the myriad number and variety of participants in the mortgage market, and the ambitious nature of HUD's proposed rule, ABA strongly urges the Department to carefully review all comments submitted, to revise the proposed rule, and to re-propose the rule. Doing so will give all participants in the mortgage markets a fair chance to respond and, ultimately, to adjust to any new system which is enacted.

The proposed rule seeks to replace the current mortgage process with two alternatives - the revised Good Faith Estimate process, and the Guaranteed Mortgage Package process. The revised GFE attempts to refine the current process, while the GMP creates an entirely new alternative for lenders, borrowers and settlement service providers. Both may well have merit, but both raise very serious issues of workability, consumer confusion, cost, and the ability of all types of lenders to compete fully in the changed marketplace. While unanimous agreement is unlikely in such a complex area, ABA believes it is critical that a broad-based consensus be achieved among participants in the mortgage process, or the reform effort is unlikely to be successful. ABA details its concerns and suggestions in the following pages.

Background

HUD issued this proposed rule in the context of extensive public discussion and review of issues relating to mortgage lending and the settlement process. HUD's discussion and intensive analysis of the role of mortgage brokers during the 1995-1996 negotiated rulemaking on mortgage broker fees and disclosures laid the groundwork for the mortgage broker component of this proposed rule. This was followed by HUD's 1999 and 2001 Statements of Policy clarifying the legality of lender payments to mortgage brokers. HUD and the Federal Reserve Board issued a joint report on reforming RESPA in 1998, which provided the basis for some of the concepts contained in this proposed rule. Also, HUD closely monitored the activities of an informal organization known as the Mortgage Reform Working Group consisting of representatives from lenders, mortgage brokers, other settlement service providers, and consumer groups. Although the group never reached a mortgage reform consensus, it did provide a forum for open discussion of mortgage reform concepts. The ABA actively participated in all of the above efforts to reform RESPA.

In terms of an overview of the proposed rule, HUD seeks to clarify the compensation and role of mortgage brokers and the role of loan originators, to redesign the GFE in terms of consumer disclosure of costs and to restrict any deviation in those costs at closing, and to provide a regulatory framework to allow guaranteed settlement service packages with exemption from RESPA's Section 8 liability.

GFE

The proposed rule requires that mortgage brokers as well as financial institution loan originators describe their services in boilerplate language on the GFE. This would state that the best rates and terms are not guaranteed and comparison-shopping would be advantageous.

The GFE would provide information to consumers regarding options available to them for payment of settlement costs through cash at settlement, through additional borrowing, through a higher interest rate or through discount points. The GFE would disclose total origination charges of the mortgage broker and the lender. Yield spread premiums and other payments by the lender to the mortgage broker would be listed on the GFE as lender payments to the borrower. Mortgage brokers would disclose the maximum amount of compensation they would receive.

HUD proposes a dramatic restructuring of the GFE in terms of its format, content, and objective. The GFE format would be reorganized "to facilitate borrower shopping for mortgages by making the mortgage transaction more transparent and to prevent unexpected charges to the borrower at settlement." HUD believes that this would discourage the use of "junk fees." The major proposed GFE categories are (1) loan originator, lender required and selected third party services, (2) title services and title insurance, (3) shoppable lender required third party services and (4) other charges such as government charges, escrow, per diem interest, hazard insurance and owner's title insurance. Dependent on the category, there would be 0% tolerance for the settlement costs at closing or a 10% tolerance. There would be no tolerance for number (1) above and for government charges except in the case of "unforeseeable and extraordinary circumstances" such as disaster or war. The 10% tolerance would basically apply to number (3) above as well as borrower selected title services, title insurance, and escrow. The tolerance does not apply to situations in which the consumer selects a provider independent of the originator's recommendation or where the consumer selects a more expensive service than required.

The GFE will include the loan amount, interest rate with APR and mortgage insurance, if applicable, and the monthly payment. There would be a statement that the interest rate could change unless locked.

The GFE would continue to be provided within three days of application but the definition of application would be changed. The redefined application would exist when basic information is provided to the originator so as to enable the originator to make an initial credit decision. Requests would not have to be exclusively in writing but could be communicated verbally or by computer. The GFE would be valid for at least 30 days. Any fee that relates to an application would be limited to the cost of providing the GFE and could not include appraisal or underwriting costs.

GMP

The GMP would provide a safe harbor from Section 8 of RESPA for anything within the package. HUD's proposed rule would remove regulatory barriers so as to encourage these packages.

The GMP could be offered by anyone who could qualify as a packager. If the packager is a non-lender, the packager must have the lender's signature verifying that the lender will provide the loan.

To qualify for exemption from Section 8 for all services within the GMP, the packager would have to offer within three days of application, a guaranteed cost for origination to include application, origination, underwriting, appraisal, pest inspection, flood determination, tax review, title service, title insurance, government fees and all other lender required services. The package would have to include the mortgage loan with interest rate guarantee subject to change only based on an "observable and verifiable index." The packager could not charge for the preparation and delivery of the package and it would have to remain open for at least 30 days. When the consumer accepts the package, the GMP becomes a binding contractual commitment subject to a "minimal engagement fee" and final underwriting and appraisal.

In terms of other costs not subject to the guarantee, there is a 10% tolerance for escrows, which must be disclosed on the GMP. Also, borrowers' choice costs such as hazard insurance, per diem interest and owner's title insurance could be excluded from the GMP and would not be subject to a tolerance. Specific services in the GMP would not have to be identified by service or cost. However, pest inspection, appraisal and lender's title insurance would have to be identified to the consumer if the lender does not plan to require any one of them. Upon request, the pest inspection, lender's title insurance, appraisal and credit reports would have to be provided the consumer.

Mortgage Servicing

In the proposed rule, HUD indicated it intends to implement by final regulation a 1997 statutory revision to the RESPA mortgage servicing transfer section. This language eliminates the requirement that a financial institution disclose the historic context of its mortgage servicing experience and a projection for the future. Prior to this finalization, HUD advised that the language of the statute may be followed in lieu of the final rule.

ABA Position

HUD's Effort on RESPA Reform

The ABA recognizes HUD's significant effort to develop a proposed rule, which HUD believes will reform RESPA by facilitating shopping for mortgage loans, by providing more meaningful disclosures and by creating a GMP designed to simplify and reduce costs associated with the settlement process. HUD's proposed rule reflects the commitment of HUD Secretary Mel Martinez to achieve these goals while enhancing the affordability of housing for individuals throughout the United States.

Secretary Martinez emphasized this commitment to the mortgage reform process during his recent testimony before the House Financial Services Committee. In his remarks, Secretary Martinez stated that, "By reforming the rules governing the purchase and finance of a home, we will create new opportunities for first-time homebuyers, keep the American dream of homeownership alive for more families, and inspire greater public confidence in the mortgage lending industry." The ABA supports the Secretary in his commitment to accomplish these objectives and looks forward to continuing to work with HUD to make this a reality.

An example of such a joint effort between the ABA and HUD could be an ABA working group to assist HUD in developing a more streamlined and concise GFE and GMP agreement. Since bankers currently work with consumers thousands of times a day in providing and explaining the GFE and the HUD-1, they are well versed in what consumers will best understand. ABA would welcome the opportunity to participate with HUD in such an effort.

As HUD seeks to attain these objectives through the RESPA reform process, the ABA urges HUD to recognize the significant regulatory burden imposed on banks by RESPA's detail and complexity. HUD should continue to reduce unnecessary regulatory burden on banks while streamlining the paperwork required by Regulation X which frequently only serves to confuse consumers rather than enlighten them.

Regulators' Oversight of Banks

HUD should recognize that banks are subject to intensive examination by their chartering and/or supervisory agencies and those agencies not only extensively examine banks for safety and soundness concerns but also oversee their compliance with numerous statutes and regulations such as RESPA and Regulation X. Banks undergo intensive scrutiny during this process. Many participants in the mortgage process that are not banks, their subsidiaries, or affiliates never receive such a thorough RESPA review. As it proceeds with a proposed rule, HUD should ensure that banks not endure additional regulatory burden because other participants in the mortgage process do not undergo such a thorough and frequent examination process.

Also, HUD should keep in mind that bank regulatory agencies have a stake in the process as they examine the institutions they regulate for compliance with RESPA and Regulation X and for any safety and soundness implications that may occur because of HUD's proposed changes to Regulation X. It is imperative that HUD coordinate the Regulation X amendment process with bank regulators. Also, HUD should ensure that the bank regulators are fully informed as to the details of the proposal process so that they are better able to examine banks under any new RESPA framework.

Adequate Lead-time for Implementation

As it moves toward further consideration of the proposed regulation, HUD should ensure that there is sufficient lead-time before any final regulation is fully implemented. As identified above, this lead-time is essential to ensure that the bank supervisory agencies are fully conversant in the final regulation and are trained to examine for its implementation. This is a key reason why ABA encourages HUD to revise the proposed rule and re-propose it – to ensure adequate input from all market participants and their regulators.

If the changes proposed by HUD, especially modification of the GFE, were to become final it would necessitate the banking industry's expenditure of extensive resources and time to become fully compliant. Banks would have to modify their mortgage origination policies and practices. They would have to retrain their employees involved in the mortgage process as well as those overseeing compliance with RESPA and Regulation Z. They would have to redesign their software programs to accommodate the changes incorporated in such a final regulation. They would have to restructure their marketing and compliance programs. If appropriate, they would have to work with their mortgage related vendors to ensure that they are in full compliance. This process is not a simple undertaking and would necessitate a significant expenditure of bank resources.

The ABA recommends that HUD establish at least a two-year period from the date a final regulation is published in the Federal Register until it becomes fully effective. Only such a time period will allow all parties affected by the final regulation to make the adjustments in policy and practice to fully comply with the modifications to Regulation X.

Redundant Language and Disclosures

The ABA strongly urges HUD to eliminate redundant language and disclosures that are already addressed in existing law and regulations especially the Truth in Lending Act ("TILA") and Regulation Z and to ensure that HUD's use of significant words and phrases that are defined in other Federal regulations is consistent with those regulations. To do otherwise would only serve to confuse consumers and impose potential roadblocks in the settlement process. Also, inclusion of items in the proposed rule relating to RESPA disclosures, which are already separately provided to consumers, only adds to a consumer's burden of understanding the complexities of the mortgage and settlement process and could result in unnecessary and expensive litigation.

As an example, the ABA directs HUD's attention to those disclosures already promulgated by the Federal Reserve Board ("Board") which underlie TILA.

In Section 3500.7 of the proposed rule, HUD intends to incorporate in the proposed GFE loan terms which are within the purview of Regulation Z and the Board.

Specifically, this section requires disclosure of:

- Loan amount
- Interest rate used to calculate the estimated amounts
- Annual Percentage Rate ("APR") including mortgage insurance
- Monthly payment for principal and interest and mortgage insurance
- Whether the loan is an adjustable rate mortgage
- Whether the loan contains a prepayment penalty clause
- Whether the loan has a balloon payment.

These disclosures are also contained in Parts II and V of Appendix C of the proposed rule, which relates to the "Instructions for Completing the Good Faith Estimate."

The ABA appreciates HUD's attempt to incorporate aspects of the two documents to seek to facilitate better understanding of important mortgage loan terms and costs. However, ABA concludes that, as proposed, HUD's loan term provisions, as above, are inappropriate and will be confusing to the consumer and draw attention away from important disclosures unique to the Good Faith Estimate. ABA suggests that HUD defer to the Board, as Congress mandated, with regard to loan term disclosures.

In this regard, HUD should recognize that disclosure of mortgage loan terms is not the purview of RESPA or Regulation X. Congress assigned that role to TILA and its implementing regulation, Regulation Z, promulgated by the Board. The proposed rule is contrary to the intent of both statutes. Also, the proposed rule preempts Congress's decision that certain terms are important and should be segregated and highlighted, as delineated in TILA.

Section 102(a) of TILA provides:

> It is the purpose of this title to assure a meaningful disclosure of credit terms so that the consumer will be able to compare more readily the various credit terms available to him and avoid the uninformed use of credit. . .

In contrast, RESPA's purpose, with regard to mortgage terms is to "effect certain changes in the settlement process for residential real estate that will result (1) in more effective advance disclosure to home buyers and sellers of *settlement* costs. . . " 12 USC 2601 (b)(1). (Emphasis added.)

Clearly, Congress intended TILA to govern loan term disclosure and RESPA to cover settlement costs. However, the proposed rule preempts this intention by mandating disclosure of certain loan terms, including those related to costs, prepayment penalties, balloon payments, and adjustable rate mortgages. The proposed rule includes these terms notwithstanding that TILA and Regulation Z specifically address these loan terms. Even more importantly, the proposed terms are in some cases inconsistent with Regulation Z.

In addition, the proposed rule fails to recognize Congress's and the Board's conclusions regarding the relative importance of loan terms. TILA and Regulation Z identify certain mortgage terms that are required to be highlighted and segregated to ensure that borrowers notice the most important terms. The proposed rule provides a different and partial list of important features in a different format that makes them less noticeable.

TILA and Regulation Z require a list of terms to be disclosed in a required form. The TILA list is more expansive than the proposed rule, which is in parts redundant of, in parts different from, TILA. Section 122 of TILA and Section 226.17(a) of Regulation Z require that the terms be disclosed "clearly and conspicuously" and that the terms annual percentage rate and finance charge be disclosed more conspicuously than other terms (except for the creditor's identity). Also, under Section 226.17(a) of Regulation Z, the required disclosures must be grouped together, segregated, and may not contain any information not directly related to the disclosures.

The proposed rule provides only a partial list of the TILA terms and reflects a decision that, contrary to the conclusions of Congress and the Board, certain loan terms contained in the proposed rule are more important than others: it excludes many important terms contained in the TILA list, such as the finance charge, which TILA requires be more conspicuous than other terms; it obscures the APR, which Congress also required to be highlighted.

It also adds new disclosures and calculations. For example, it requires disclosure of the APR and the percentage attributable to mortgage insurance. While mortgage insurance costs are otherwise incorporated into the TILA disclosures, the percentage attributable to mortgage insurance is not a required disclosure. There is no explanation of why this new disclosure is being added by HUD when the Board, which has jurisdiction over loan terms, has not deemed it necessary.

Rather than reinforcing by repetition, ABA believes that the proposed rule will confuse consumers because terms are inconsistent and redundant. It will also distract consumers from noticing important terms, such as the APR because, as unhighlighted terms in a long series of disclosures, they will fade into the document. Unnecessarily lengthening the form with redundant terms will also mean that consumers will be less likely to read the materials more carefully, if at all. ABA is also concerned that those providing the disclosures will be tempted in good faith to direct borrowers to the RESPA document, on the basis that it contains all the important terms, including many of those contained in the TILA documents.

The proposed rule also illustrates the difficulty of defining and formatting loan terms in an effective fashion, another reason to defer to the agency with the background, history, and authority for the task. To illustrate, Section 3500.7 of the proposed rule requires disclosure of the "loan amount." The proposed Appendix C and its instructions refer to the "mortgage amount." Are these terms the same? Are they the same as the "amount financed" as defined by Regulation Z? Do they include "any other amounts that are financed by the creditor and are not part of the finance charge" as Regulation Z defines amount financed?

The proposed rule, Appendix C, and its instructions all appear to envision a different version of payment disclosures. The proposed rule requires disclosures of the **"monthly payment for principal and interest and mortgage insurance,"** as prescribed in Appendix C. (Emphasis added.) Appendix C instructions prescribe disclosure of the length of the loan and the **"monthly payment, including any mortgage insurance."**(Emphasis added.) Are these terms the same? Does the "monthly payment for principal and interest" required by the proposed rule exclude other amounts, such as other finance charges, that are part of the borrower's monthly payment? How do these two terms differ from the TILA payment schedule disclosures?

The proposed Appendix C requires disclosure of the term of the loan (in years), the number of monthly payments, and the initial payment of principal and interest and mortgage insurance. It does not appear to contemplate disclosure of the amount of payments made after the initial payment, which may vary from the initial payment. This commonly happens, for example, with the last payment, which may be modestly more or less than the usual payment. It also happens with balloon payments. However, Appendix C does not contemplate any variations in monthly payments. Appendix C is not labeled a "model" form. Is it mandatory? How do lenders reconcile the contradictory instructions?

The proposed rule requires disclosure of the interest rate. The proposed Appendix C uses the phrase "[fixed] interest rate." Why is "fixed" in brackets if the disclosure contemplates referring those with adjustable rate mortgages to a separate section?

Part V of the proposed rule requires disclosure of the initial interest rate and how often the rate will change, but does not appear to anticipate adjustable rate mortgages with a discounted or "teaser" rate or loans that have stepped up interest rates. The proposed disclosure, in fact, would be misleading because it does not highlight that the interest rate will increase significantly in the first month or other period.

How does a lender disclose an Alternative Rate Mortgage ("ARM") with an initial discount rate using the proposed required disclosure? This is illustrated in Section V of the proposed GFE as follows:

> The initial interest rate for this ARM loan is __ %. The first adjustment will occur after __ months/years and every month/year thereafter for a period of __ years. The interest rate is based on the __index and may increase by a margin of __% over the index with each adjustment. The maximum rate increase adjustment per period is __% and the maximum interest rate that can ever apply to this loan is __%.

As identified above, the proposed rule does not require disclosure of the amount of the increase after the initial discounted rate. Moreover, the proposed language is again inconsistent with Regulation Z, which requires disclosure of the APR. This term includes other finance charges beyond interest.

It is imperative that the terms of RESPA and TILA and their definitions be consistent, both for the interests of consumers and lenders. As it is now, the proposed rule is fraught with inconsistencies that will confuse consumers so that they are more likely to ignore them than endeavor to reconcile them. It will also be a minefield for lenders trying in good faith to comply with the competing disclosures.

Given the Board's mandate to develop meaningful loan term disclosures, its successful efforts to fulfill that complicated mandate, and its long history in developing TILA disclosures, ABA strongly urges HUD to defer to Regulation Z and the Board with regard to loan terms disclosures.

Attachment A-1

Also, the proposed rule requires that in the case of a GMP the lender identify on Attachment A-1 that certain specific services are or are not required. The lender must disclose that the reports generated by these services must be available to the customer upon his or her request. The services subject to this requirement are the pest inspection, lender's title insurance, property appraisal, and credit report.

The ABA recommends that HUD delete this proposed requirement from its final rule. The availability of property appraisal reports and credit reports are fully addressed by other statutes and HUD should defer to the Federal agencies responsible for these disclosures. Also, ABA recommends that HUD delete the pest inspection and lender's title insurance reports from this requirement as an unnecessary disclosure, which only adds to the paperwork provided the customer.

The Equal Credit Opportunity Act ("ECOA") and Regulation B already address the applicant's right to a property appraisal report. Section 701 (e) of ECOA requires creditors to provide copies of these appraisal reports and directs the Board to adopt regulations implementing this statute. Accordingly, Section 205.5a of Regulation B requires lenders to provide a copy of the appraisal report, but also allows various options that included notices of the right to the report or automatic delivery. First, HUD should leave regulations regarding access to appraisal reports to the federal agency assigned the task, in this case, the Board. The Board has identified the appropriate disclosures and timing of disclosures after extensive public comment. This process works well and ABA is not aware of any complaints relating to the provision of property appraisal reports.

Second, ABA does not believe that repeating a particular item, especially one that is not deemed highly important to the shopping decision, enhances the disclosures, especially among so many other important terms and disclosures. As noted earlier, this confuses consumers and lengthens the disclosure so that they are less likely to review carefully what they receive.

Similarly, the proposed notice regarding credit reports reaches beyond the requirements of the Fair Credit Reporting Act ("FCRA") and assumes jurisdiction of a matter Congress assigned to other agencies.

Section 615 of the FCRA requires that if a credit report is used in making an adverse credit decision, (which includes a denial or rejection of terms not as requested) the lender must provide notice of that fact along with notice of the applicant's right to obtain a free report. Moreover, in 1996, when Congress amended FCRA substantially, it chose to address consumers' access to reports by, for example, *permitting* users of a consumer report to share it with an applicant *in the event the report was used for adverse action.* (Emphasis added.) The proposed rule clearly goes beyond what the statute dedicated to credit reports requires by *mandating* that *creditors* provide the report upon request. (Emphasis added.) Congress had the opportunity to adopt a HUD-like proposed requirement in 1996, after years of debate about amending FCRA, but chose not to do so.

In the case of banks, only the federal banking agencies are allowed to prescribe regulations under the FCRA. In general, the federal banking agencies, the Federal Trade Commission, and the states, not HUD, are responsible for enforcing that statute with respect to all types of lenders.

The ABA also recommends deletion of the right to the pest inspection and lender's title insurance reports. First, ABA does not believe there is value in providing this disclosure or these reports: their utility was not explained in the supplementary information other than to explain that they are of "specific interest and value to the borrower." (67 Federal Register 49153, July 29, 2002). These services are intended to provide information to protect the lender, not the borrower. They assure the lender that the property on which the lender is relying as a security interest will not be threatened by physical deterioration or superior legal claims. They are accordingly priced and delivered for this purpose. Furnishing them to consumers could lead consumers to rely on them for their own purposes and provide a basis for an unanticipated lawsuit. Prices and contracts would have to be adjusted to reflect this.

Second, the disclosures will unnecessarily lengthen the disclosure forms, distracting consumers from more important information and discouraging them from reviewing the document altogether. Finally, ABA does not believe that HUD has the authority under RESPA to mandate the provision of these reports. Thus, ABA recommends deletion of this provision.

Application

The ABA is also concerned that the definition of application, when coupled with the requirements to guarantee terms either subject to or not subject to tolerances in effect dictates the factors lenders can consider in pricing mortgages.

For example, the proposed rule defines application to mean:

> the submission of credit information (Social Security number, property address, basic income information, the borrower's information on the house price or a best estimate on the value of the property, and the mortgage loan needed by a borrower in anticipation of a credit decision…

The proposed rule further requires that the GMP guarantee the interest rate and APR. In effect, the proposed rule mandates pricing criteria by limiting the information required on an application on which the lender must base a pricing decision. Simply put, it obliges creditors to price loans based on the criteria set forth in the proposed rule.

The proposed rule ignores factors both commonly and occasionally used today to price mortgage loans: e.g., assets of borrower, current rent payment, whether the property is a condominium or coop. There are undoubtedly other factors, particularly for programs designed to be more flexible in underwriting and pricing standards in order to broaden the field of eligible borrowers and provide more affordable loans. The proposed rule in effect precludes lenders from using these factors as well as other factors that lenders in the future may determine are appropriate and useful for pricing loans. ABA does not believe that HUD should be dictating pricing criteria.

Instead, the proposed rule should look for guidance at definitions of "application" contained in Regulation B and Regulation C. Section 202.2(f) of Regulation B defines application as "an oral or written request for an extension of credit that is made *in accordance with procedures established by a creditor* for the type of credit requests." (Emphasis added.) Under Section 203.2(b) of Regulation C, application means "an oral or written request for a home-purchase or home-improvement loan that is made *in accordance with procedures established by a financial institution for the type of credit requested.*" (Emphasis added.) These definitions allow lenders to establish their own criteria for evaluating creditworthiness and loan terms (except for prohibited basis as defined under ECOA.) This approach to defining applications is more appropriate in the context of the proposed rule and will facilitate compliance by making the terms consistent.

If HUD does not modify the definition, it should eliminate the requirement to guarantee an APR and interest rate. Lenders should not be required to price loans without adequate and appropriate information.

However, the proposed rule should retain the reference to "submission of credit information" or a similar phrase and avoid the Regulation B and Regulation C references to request for credit. Otherwise, the shopping inquiry envisioned under the proposed rule could trigger unwanted Regulation B notices and Regulation C reporting requirements.

<u>GMP</u>

Throughout the mortgage reform discussion process, ABA has recognized the interest of many banks in the concept of a Guaranteed Mortgage Package. In developing such a package, the ABA has recommended to HUD that it structure such a package so that it would serve as an optional approach to the traditional GFE. Such an option would provide the broadest range of choices to banks in terms of the mortgage products that they offer and to consumers in terms of which products are in their best interest.

In this context, the ABA believes that the concept of the GMP may be a viable option for lenders, provided that the GFE and the fee for services rendered approach to the mortgage process remain an equally viable option for banks.

In terms of the specifics of the GMP as proposed by HUD, the ABA has several recommendations that would restructure the GMP so as to better reflect the realities of the marketplace.

HUD should delete the word "guaranteed" from the package, as it implies a lock on costs, contrary to the intent of the proposed regulation. A more appropriate word or phrase should be substituted. While the goal of an all-in package at a set cost is laudatory, the fact remains that a number of items may not be able to be included in a package, which would lead to confusion by consumers if the package were referred to as a "guarantee."

Mortgage originators should be allowed to collect a fee for the GMP that is sufficient to cover the costs of the initial credit determination process. The proposed rule sets forth that originators may only collect a "nominal" fee at application. A "nominal" fee raises a number of questions – the most serious of which is how HUD will determine what is "nominal" especially in light of the fact that RESPA specifically directs that HUD not set prices for settlement services. Rather than venture into such troubling territory, ABA suggests that HUD simply require that the fee collected by originators should cover the initial credit determination efforts of originators.

The mandatory shopping period, set by the proposed rule at not less than 30 days, should be reduced to not less than 10 days. Requiring an originator to hold rates and terms open for an entire month is an excessive burden, which may reduce options for consumers as it creates uncertainty and unnecessary delay in the marketplace. A 10-day shopping period provides borrowers with ample time to shop among various originators, while ensuring that originators do not unnecessarily tie up lines of credit for loans which may never be made.

Finally, HUD should provide for a "cure" mechanism for technical violations of the GMP. In the fast-paced environment of mortgage origination, it is inevitable that unintended errors will be made. Those offering the GMP should be provided with the ability to cure errors before being penalized for those errors. ABA strongly encourages HUD to add a "cure" mechanism.

<u>GFE</u>

Many banks have expressed to the ABA their serious concern with the proposed revised GFE. To them, HUD's proposed modifications to the GFE convert what for years has been an estimate of settlement costs to a new, expanded form which is very close to a guarantee of settlement costs. The proposed revised GFE does not offer banks and other lenders a viable option to the GMP since it imposes new requirements on lenders which, many believe, transcend the intent of Congress in requiring "a good faith estimate of the amount or range of charges for specific settlement services the borrower is likely to incur…" Many believe that such statutory language precludes HUD from imposing the changes incorporated in the proposed revised GFE. For decades, bankers have effectively served their mortgage loan customers and to the best of their knowledge have provided accurate and complete estimates of anticipated settlement costs in the form of the GFE. They believe that imposing strict tolerances recommended by HUD will interfere with their ability to serve their customers and will discourage them from future mortgage lending activity.

The ABA's members have identified several aspects of the proposed revised GFE, which create potential problems. The ABA joins with banks throughout the country in raising these issues. Their concerns include (1) the above-mentioned tolerances, which fail to take into account local variations in the settlement process and costs that might well exceed the best intentioned estimate, (2) the need to reduce the complexity of the proposed revised GFE by eliminating information otherwise included in other disclosures and/or incorporating this additional language in HUD's Special Information Booklet, (3) the problems created by requiring banks to maintain the estimates identified in the GFE for a minimum of thirty days, and (4) the problems associated with the imposition of restrictions on the ability of lenders to modify mortgage products available to their customers resulting in application denials and multiple re-issuances of the GFE.

In particular, the proposed revised GFE requires that certain terms may "not vary at settlement by greater than a tolerance of 10% from the amounts for such categories reported on the good faith estimate…absent unforeseeable and extraordinary circumstances." These include, for example, lender required and selected third party services. "Unforeseeable and extraordinary circumstances," defined as "act of God, war, disaster, or any other emergency making it impossible or impractical to perform" obviously has a very limited application.

This requirement will unfairly require lenders to absorb necessary costs. For example, property appraisals and surveys are subject to a strict tolerance. However, there are occasions when these fees are unexpectedly and significantly higher than usual. For example, the property may be unusual or difficult to reach or evaluate, e.g., property is difficult to access due to road conditions, and property contains difficult terrain or other obstacles such as animals. The appraiser must therefore expend much more time on the valuation, resulting in a fee that can be three or four times higher than "usual." Lenders with a significant volume of business in mortgage loans may be able to absorb the loss, but the additional burden will force other lenders to reconsider whether to offer such loans, especially those that make only a few mortgages a year as a customer convenience.

The ABA urges HUD to carefully consider these and the other concerns raised by banks relating to the proposed revised GFE. HUD should use the re-proposed rule as an opportunity to make modifications to ensure that the revised GFE is a workable document and a realistic option for banks.

Mortgage Servicing Transfer Disclosure

In the preamble to the proposed rule, HUD indicates that it intends to finalize the 1997 Congressional modification to the Mortgage Servicing Transfer Disclosure language of RESPA. ABA fully supports HUD in its implementation of this statutory change. ABA urges HUD to issue a regulation implementing this change separate and apart from action on this proposed rule. ABA recognizes that HUD has indicated that the statutory language addressed by this change may be used in lieu of the existing language of Regulation X. However, for purposes of fully informing banks and other lenders of its applicability, the ABA recommends HUD act quickly to incorporate this statutory change in Regulation X.

Affiliated Business Treatment Proposal

The ABA, along with its affiliate, the American Bankers Insurance Association ("ABIA"), would also like to express our support for the eligibility of independent insurance agents and brokers to receive a fee for referring their insurance clients to the banking operations of full financial services (insurance and banking) enterprises with which they are contracted.

Essentially, the proposal aims to level the playing field between competing segments of the insurance industry in terms of the application of one specific provision in Section 8 of RESPA. This provision is applicable only to insurance carriers whose distribution mechanism is the independent agency system. Large, direct writers are advantaged in this regard since their network of "captive" agents qualifies as "affiliates" and are, therefore, exempt from this specific provision of RESPA. This proposed rule would correct this presumably unintended result, expanding options for consumers.

The ABA and ABIA ask your consideration of the inclusion of this proposal as part of a re-proposal of this rule, with the intent of achieving a more level playing field, of eliminating the unintended advantage of one segment of the financial services industry over another and of furthering expanded consumer options.

Conclusion

In conclusion, the ABA congratulates HUD for addressing comprehensive mortgage reform. The mortgage origination process is a complicated and important one, which in many instances, is the most significant transaction entered into by many borrowers. HUD is to be commended for its efforts thus far. ABA believes that real reform is possible, but that more steps are necessary to ensure that the current process is improved without unduly disrupting those elements of the system that are working. As HUD has recognized, the current mortgage process is one that has provided the highest rate of homeownership in our nation's history, and reform must be achieved carefully to ensure that the ability of consumers to obtain housing credit and services is not impinged. Therefore, ABA strongly encourages HUD to revise the current proposed rule, and re-propose it for additional comment.

If you have any questions or need additional information, do not hesitate to contact the undersigned at (202) 663-5333.

Sincerely yours,

John C. Rasmus

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Testimony of
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On Behalf of the
Appraisal Institute and
American Society of Appraisers

Before Subcommittee on Housing and Community Opportunity
Of the
House Committee on Financial Services
On

"Simplifying the Home Buying Process: HUD's Proposal to Reform RESPA"

Presented by
Alan Eugene Hummel, SRA
President, Appraisal Institute
Chief Executive Officer, Iowa Residential Appraisal Company
Des Moines, Iowa

February 25, 2003

Testimony of Alan Eugene Hummel, SRA
On Behalf of the Appraisal Institute and American Society of Appraisers
Before the
Subcommittee on Housing and Community Opportunity
of the
Committee on Financial Services
United States House of Representatives

Mr. Chair and members of the Subcommittee, I am Alan Eugene Hummel, President of Iowa Residential Appraisal Company in Des Moines, Iowa and 2003 President of the Appraisal Institute. I am pleased to be here today on behalf of the Appraisal Institute and American Society of Appraisers, which together represent more than 25,000 real estate appraisers in the United States.

I want to thank you for holding this hearing. The Department of Housing and Urban Development Proposed Rule on the Real Estate Settlement Procedures Act (RESPA) is of great importance to consumers and the financial community. This issue is also important to members of our organizations, who together constitute the leading professional organizations of appraisers in the United States.

The proposed rule on RESPA impacts real estate appraisers in two areas: 1) HUD wants lenders to provide consumers a simple, clear and firm Good Faith Estimate (GFE), at no or nominal cost, so they can better understand the charges, including appraisal costs, and use it to shop for a home loan and service providers before they become so invested in the process that they cannot back out; and 2) HUD wants to allow certain entities to assemble and offer consumers "guaranteed mortgage packages" (GMP) - a guaranteed mortgage interest rate and a guaranteed price for a complete package of settlement services, including appraisal services.

We agree with the primary goal of the proposed rule, which is to simplify and improve the process of obtaining a mortgage. There is little doubt that the volume of paperwork required to obtain a mortgage is burdensome to the homebuyer, and we commend HUD for undertaking this difficult task.

However, the proposed "packaging" of services raises the issue of proper and full disclosure of appraisal costs and appraisal services to consumers. In light of recent mortgage fraud and predatory lending cases throughout the country, we believe it is important to honor safeguards which protect homebuyers from unscrupulous actors in the residential real estate market.

Specifically, we are concerned that the proposal to package services may actually limit existing consumer protections. Secondly, the proposed rule has the potential to increase incidents of inappropriate client pressure or influence, a phenomenon that is detrimental to the lending process. This kind of influence has negative market consequences, as consumers face the financial danger of entering into a mortgage for more than the value of their new home. Finally, offering a guaranteed price for an assemblage of settlement services, or package, may lead to a shortage of qualified appraisers to perform appraisal assignments. Such a shortage would result in delays and ultimately higher costs for the consumer.

Therefore, we cannot support the rule as proposed. The following details our concerns with the proposed rule and offers specific suggestions on how to address them.

Appraisal-Related Problems with Guaranteed Mortgage Packages and Good Faith Estimate
The proposed rule would remove regulatory barriers to allow a package of settlement services to be made available to borrowers. According to HUD, these transactions, arguably, would be simpler and more transparent for borrowers, and would allow market forces, borrower shopping, and competition to further reduce the costs of settlement services. To accomplish this objective, first HUD would establish a carefully circumscribed safe harbor under RESPA for GMP transactions. Any entity (a lender, broker, other settlement service provider, or other entity), hereinafter a "packager," may qualify for the safe harbor as long as it offers a GMP. The packager must offer the GMP to a borrower following his or her submission of application information, but before the borrower's payment of any fee to the packager.

The proposed rule offered an example of how these arrangements might work with real estate appraisers in a GMP:

> "For example, a packager could contract to have XYZ Appraisal Company complete all its appraisals for a given period for $300 each rather than the $350 the company normally charges for a standard appraisal. The packager could rely on that discounted contract price in pricing the package of guaranteed costs to the borrower. With their own costs negotiated in advance, packagers could disclose the cost for the entire package early in the borrower's mortgage shopping process with certainty, and the borrower then could compare different vendors' packages."

Concern 1: Packaging is not consistent with disclosure. A fundamental goal of HUD's proposal is to protect consumers. It is our view that the packaging of services is inconsistent with the goal of seeking greater disclosures of costs to consumers.

Today, an appraisal is a vital part of home buying or refinancing. The appraiser is an independent third party delivering an unbiased opinion of value. Although the appraiser is typically hired by the lender, it is the appraiser's objectivity that helps both the lender and the consumer when entering into a financial relationship.

Although the appraisal services necessary to close a loan may be primarily for the benefit of the lender, we believe consumers benefit from an appraisal ordered by the lender as well. The proposed rule recognizes this dual function in its proposed rule, stating:

> "HUD believes however, that there are certain settlement services that are of specific interest and value to the borrower such as pest inspection, appraisal and the purchase of lender's title insurance (which may affect the cost of owner's title insurance)."

Under the GMP, the consumer will not know what kind of appraisal or valuation was performed, what was charged for those services, including whether any of these services were "marked up", and ultimately how much they are paying for these services at closing. Packaging may help simplify the process from the lender's perspective; however, the type of valuation performed and borrower's fees will be obscured. We believe the borrower deserves more protection.

There are many different types of appraisal or valuation services that can be provided during a mortgage application. Officially, an "appraisal" is the act or process of determining an opinion of value. Appraisals conform to industry-wide standards known as the Uniform Standards of Professional Appraisal Practice (USPAP) and are performed by licensed or certified professionals. Anything short of this is known as a "valuation," which can be computer assisted and performed by the lender or broker. Oftentimes valuations are performed by those that have an interest in the transaction.

Various levels of property analysis may be utilized in estimating the market value of a property. Automated Valuation Models (AVM's) are a form of computerized statistical modeling. They offer the least in human verification of real-time property condition and characteristics, as they rely primarily on public records and proprietary databases for information. AVMs are typically most reliable in areas of homogenous properties, and those that are not suffering from deferred maintenance or customized features. There are a wide variety of models in use across the U.S., with a wide range in the "confidence level" in the final value indicator. At their basic level, AVM's are operated by technicians with no valuation expertise or particular knowledge of the property they are appraising, nor the sales that are being used within the analyses. Typically the reports are transmitted in proprietary formats that vary from vendor to vendor, are limited detailing the analysis and typically not signed by an individual who could be held accountable for the conclusion.

At the other end of the spectrum is a "complete appraisal" from an individual who has been trained in appraisal analysis and methodologies and holds, at minimum, credentials from a state appraisal licensing agency with requirements for education, experience and record keeping. This professional performs a much more detailed analysis of not only the macro-economic conditions that effect property values, but the individual characteristics of the property being appraised as well as those properties that have sold. Most times, an actual viewing of the property takes place by the professional to discern if the property contains any characteristics, good (updated features such as flooring and kitchens, amenities such as pools or finished space in the lower or upper levels of the home) or bad (leaking roofs, signs of structural instabilities, location next door to detrimental conditions). Many times these factors are not available through any other source than a visual viewing of the property, and the existence of the various items may have a substantial impact on the value of the property. These appraisals are often reported on a standardized industry-recognized form, which allows for the consistent review and audit of appraisals.

We believe the type of appraisal or valuation performed and the costs associated with these services should be transparent to the consumer since the consumer is paying for the service. As HUD has recognized, the appraisal has a specific interest to the borrower, and we feel those services, and that interest, should be fully disclosed.

There is also good reason for identifying the appraiser in the documentation for the consumer, as it helps create a system of ensuring the credibility for the work product and the accountability for the appraisal fees. Withholding or obscuring this information has the potential only to harm the borrower.

Concern 2: Limiting the upfront fee a borrower pays to the lender for the cost of preparing a GFE, and encouraging packaging arrangements will **increase appraiser exposure to inappropriate client pressure**. Real estate appraisers too often face inappropriate pressure from lenders, brokers, realty agents and management companies (often owned by lenders) to produce unsupportable values that facilitate mortgage transactions.

To capitulate to such pressure, an appraiser would violate the Ethics Rule of the USPAP[1]. However, failing to deliver a predetermined value under these circumstances often results in an appraiser being labeled "difficult to work with" or ostracized by clients in the marketplace. Unfortunately, according to our members, many lenders seek out appraisers willing to conform to such unscrupulous demands.

This kind of pressure has negative market consequences, as **consumers face a greater threat of entering into a mortgage that is greater than the value of their new home**. HUD and the lending community in general also face a threat as well, as these inaccurate appraisals do not accurately reflect the value of their mortgage portfolios and thus, increase the exposure to risk. Furthermore, transactions that are consummated at sales prices above their true market value can then be used to further exacerbate the overvaluation of other homes - leading to over lending on homes that are being refinanced - not just those being transferred in ownership.

Under the proposed reforms, lenders will likely face a dilemma on when to order a credit report and appraisal. Without advance payment, lenders who order a credit report and appraisal for a given loan will be liable for these costs and face exposure to loss should the borrower not go through with the loan, which is likely to happen with greater frequency when more shopping takes place. In order to limit their exposure, lenders are likely to defer ordering the credit report and appraisal until the borrower commits to the loan, which is likely to slow down the loan process. This is contrary to the mortgage industry's desire to expedite the loan process.

[1] "An appraiser must perform assignments ethically and competently, in accordance with USPAP and any supplemental standards agreed to by the appraiser in accepting the assignment. An appraiser must not engage in criminal conduct. An appraiser must perform assignments with impartiality, objectivity, and independence, and without accommodation of personal interests." Uniform Standards of Professional Appraisal Practice, lines 258-261, p.7, 2003 Edition. Source: The Appraisal Foundation.

Lenders that are exposed to unpaid fees are more likely to exert greater pressure on appraisers to "bring in the numbers" so those loans can be made with reduced "kick out" risk. Historically, the borrower pays the appraisal and credit report fee at the time of application. Under this arrangement, the appraiser was somewhat, although not entirely, insulated from collection and lender pressure issues since the money was held in escrow by the lender.

Another possibility is that, in an effort to limit their exposure to loans that do not close, lenders and third party settlement service providers who order credit reports and appraisals early in the application process may attempt to negotiate contingent fee arrangements with vendors. Such arrangements are not allowed by USPAP and are barred in many states[2].

So that HUD can properly rely on quality appraisals to help protect the interests of lenders and borrowers, it should not encourage a system that rewards companies that use volume contracts with outside vendors to be competitive. Many of our members are concerned that these volume contracts will generate moral hazards which will result in lower quality appraisals, greater client pressure, lower financial stability for the nation's mortgage financing system and create a higher risk for consumers who may inadvertently commit to mortgages that are higher than the equity of their collateral. HUD should avoid creating a system whereby a single client provides so much business that an appraiser's economic viability would be decimated upon losing that client.

Concern 3: Many of our members are concerned that offering a guaranteed price for an assemblage of settlement services could impact many small appraisal businesses throughout the country (particularly in non-metropolitan areas), leading to a **shortage of qualified appraisers to perform appraisal assignments**. Contrary to one of the premises of the proposed rule, research shows that the appraisal component of settlement service costs has not seen a pricing increase in over a decade. In fact, appraisal fees for many services have decreased due to technology and efficiencies in the market.

Even with these efficiencies, it is not feasible for appraisers to continue to provide consistent, quality appraisals for less, especially if they are unable to charge market prices for complex assignments. Routinely, appraisers are confronted by properties that demand more of their time to complete the assignment. For example, if a property to be appraised is fronted by water or other unique amenities, it will likely require the appraiser to compile comparable sales from multiple locations and towns. Because the house and the comparable sales are not ordinary, the appraiser must talk to someone familiar with the property to find out particularly distinguishing data. This type of complex residential appraisal assignment

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[2] "It is unethical for an appraiser to accept compensation for performing an assignment when it is contingent upon: 1) the reporting of a predetermined result (e.g., opinion of value); 2) a direction in assignment results that favors the cause of the client; 3) the amount of a value opinion; 4) the attainment of a stipulated result; or 5) the occurrence of a subsequent event directly related to the appraiser's opinions and specific to the assignment's purpose." Uniform Standards of Professional Appraisal Practice, lines 287-294, p.8, 2003 Edition. Source: The Appraisal Foundation.

would require greater staff hours to complete, thus warranting a fee that can be significantly higher than the standard appraisal fee.

The proposed rule outlines a one-size-fits-all concept of a 10 percent tolerance, or upper limit, on charges provided by third-party service providers. This tolerance is too restrictive. When extra costs result from an atypical appraisal assignment, the appraiser should be able to recoup the expense.

While market forces are currently lowering appraisal costs, the proposed rule appears to create a disincentive to perform mortgage appraisal assignments. Our members are concerned that the proposed rule may ultimately encourage existing appraisers to decrease mortgage appraisal work and would discourage new appraisers from entering the profession. In an effort to keep appraisal costs down and maintain the availability of appraisers throughout the country, HUD should enact policies that encourage a larger pool or participants, not a smaller one.

RESPA Suggestions
To address these concerns, we offer the following suggestions:

Suggestion 1: Since packaging hides the type of valuation performed and obscures fees paid for valuation services from the consumer, **we encourage HUD to keep the contract appraisal fee under the GFE and out of the GMP**. Instead, we recommend that only the lender's charge for reviewing or administering the appraisal function be included in the GMP, not the amount paid to a contracted appraiser.

Under our recommendation, the fee that is paid to the contracted real estate appraiser would not be included with application, origination and underwriting services and any other lender required services or other fixed fees. This suggestion would allow the contract appraiser to be considered an entity outside of the GMP package. It is our view that a GFE disclosure is adequate for consumers, in particular if the costs are itemized. Under these circumstances, the consumer could be given a copy of the contract appraiser's invoice at closing to document the actual cost of service. Lender fees for appraisal administration would then be transparent, and could subsequently be compared to the quotes in the GMP package. At the same time, it is likely that the "price point" of the appraisal services will continue to decline if it is not in the GMP because of market forces and technology. HUD should allow these natural market forces to work.

We do not recommend doing away with the GMP proposal altogether. We simply call for the rule to be modified to allow for full disclosure of the appraisal fees, which HUD has admitted is of interest and value to the consumer.

Suggestion 2: **HUD should include language in the final rule that prohibits client pressure, make such policies accessible to appraisers, and require lenders to pay for all third-party services regardless of loan status.** The proposed packaging of services will concentrate significant purchasing power among the largest national financial institutions and management companies. Coupled with the proposed requirement that definitive, upfront fee schedules be provided to prospective borrowers, these national purchasers of appraisal services will be able to exert unbridled pressure on independent fee appraisers. Therefore, it is critical that safeguards be included in the proposed RESPA final rule that squarely address the most critical and vulnerable areas for the appraisal community - client pressure and contingent fees. Both of these practices should be prohibited in the final rule through the inclusion of clear and unambiguous language.

HUD Mortgagee Letter 94-54 contains a section on "Pressure on Appraiser and Conflicts of Interest." This section states:

> "The Department requires that appraisers chosen under this new procedure not be supervised or directed by any loan officers or loan production personnel. Chosen appraisers should be supervised by the lender's underwriting or management personnel. Instances of undue pressure or influence on an appraiser reported to HUD will result in appropriate disciplinary actions against the lender involved."

Although we are pleased HUD has accepted that undue pressure of appraisers exists, we feel it could do much more by providing more information to appraisers on the existence of HUD's requirements. Most appraisers are simply unaware that HUD will accept complaints against lenders applying undue pressure. Typically, they do not know whom to contact within HUD, and HUD has established no procedure on how the appraiser is to submit his/her complaint.

We encourage HUD to establish a system that informs appraisers of HUD's requirements relating to inappropriate client pressure on appraisers and establishes common procedures for conducting investigations of complaints issued by appraisers. Such procedures would tell the appraiser what information must be provided in the complaint and whether HUD will hold the appraiser's identity in confidence during the investigation. HUD could even establish a "hotline," or clearly specify a staff member who could handle such investigations and make this known to licensed and certified appraisers. HUD, when receiving these complaints, should provide sufficient resources to conduct thorough investigations and conduct effective enforcement activities.

HUD should also prohibit any and all contingent fee arrangements in connection with appraisals. We recommend language be included in the final rule mirroring comments in the Management section of the Ethics Rule of USPAP wherein it is recognized that it is unethical for an appraiser to accept compensation for performing an assignment when the assignment is contingent upon (1) the reporting of a predetermined result; (2) a direction in assignment results that favors the cause of the client; (3) the amount of the value opinion; (4) the attainment of a stipulated result; and or (5) the occurrence of a subsequent event directly related to the appraiser's opinions and specific to the assignment's purpose. Including the above language in the proposed RESPA final rule would parallel what is now part of most state law.

Suggestion 3: HUD should create an exemption for loans secured by historic and high-value or otherwise atypical properties with the requirement for accurate GFEs. A "one-size-fits-all" approach to packaging is likely to lead to greater standardization of fees for appraisal services. Such standardized fees will not allow for the premiums that are warranted for complex appraisal assignments.

Since the appraisal fee must be communicated to the borrower by the financial institution very early in the relationship, time will not allow for fees to be reflective of such premiums that are typically charged for complex residential appraisal assignments - e.g., historic properties, high-value residences, etc. So as to not stifle the public's ability to use these types of properties for collateral, the proposed RESPA final rule should contain a "carve out" provision that allows more flexibility with fees that need to be charged for these types of unique appraisal services.

About the Appraisal Institute and American Society of Appraisers
The Appraisal Institute is the acknowledged worldwide leader in residential and commercial real estate appraisal education, research, publishing and professional membership designation programs. Its extensive curriculum of courses and specialty seminars provides a well-rounded education in valuation methodology for both the novice and seasoned practitioner. Members of the Appraisal Institute form a network of highly qualified professionals throughout the United States and abroad. They are identified by their experience in and knowledge of real estate valuation and by their adherence to a strictly enforced *Code of Professional Ethics and Standards of Professional Appraisal Practice.*

The American Society of Appraisers is an organization of appraisal professionals and others interested in the appraisal profession. International in structure, it is self-supporting and independent. The American Society of Appraisers is the oldest and only major appraisal organization representing all of the disciplines of appraisal specialists, including real property. ASA is diligent in its efforts to strengthen and uphold the *Principles of Appraisal Practice and Code of Ethics* in order to protect the client.

We appreciate this opportunity to provide our official comments for the record. Should you have any questions, please contact Don Kelly, Vice President of Public Affairs, Appraisal Institute at 202-298-5583, dkelly@appraisalinstitute.org or Ted Baker, Executive Vice President, American Society of Appraisers at 703-733-2109, tbaker@appraisers.org.

Testimony of the

Consumer Bankers Association

on

Simplifying the Home Buying Process:

HUD's Proposal to Reform RESPA

before the

Subcommittee on Housing and Community Opportunity

of the

Committee on Financial Services

of the

United States House of Representatives

on

February 25, 2003

The Consumer Bankers Association (CBA) appreciates this opportunity to submit our views regarding the efforts of the U.S. Department of Housing and Urban Development (HUD) to reform the regulation implementing the Real Estate Settlement Procedures Act (RESPA). We have attached to this brief statement our more complete comments that were provided to HUD during the rulemaking process, and we appreciate your including them in the record along with this testimony.

The Consumer Bankers Association is the recognized voice on retail banking issues in the nation's capital. Member institutions are the leaders in consumer financial services, including real estate-secured lending covered by RESPA. CBA members include most of the nation's largest bank holding companies as well as regional and super community banks that collectively hold two-thirds of the industry's total assets.

Today we wish to restate our support for simplification and reform of the RESPA mortgage lending process. In particular, we support HUD's bold and innovative proposal to permit lenders to offer a Guaranteed Mortgage Package (GMP) within three days of an inquiry (in place of the Good Faith Estimate of closing costs). A GMP would include a guaranteed lump-sum amount of settlement costs (including all lender required settlement services except per diem interest, hazard insurance, and escrow/reserves). Those lenders who offer a GMP would be entitled to an exemption from RESPA's section 8 prohibitions on referral fees for settlement service costs within the GMP package. If the customer accepts the offer, the lender would be contractually bound not to charge more than the GMP Agreement (GMPA).

We agree with HUD that the GMP concept is an appealing option for many lenders, since it will permit them to negotiate packages at favorable costs. Consumers will also benefit because they will be provided a "guaranteed" price upon which to shop for the best terms. In fact, CBA was an early supporter of this concept, because we believe it will reduce the complexity of disclosures, provide useful shopping information at a more advantageous time for consumers, allow market forces to keep costs down, and reduce the chance of the consumer being surprised by settlement costs at closing.

Notwithstanding our general support, we must also state some concerns regarding HUD's proposal. First, we believe it is a mistake for the proposal to prohibit HOEPA (or "high-cost mortgage") lenders from using the GMP option. If HUD is correct that this proposal will be beneficial to consumers, it should be available for use with HOEPA loans as well. Creating a competitive marketplace where consumers can shop for credit would go a long way toward eliminating predatory lending practices in the high-cost mortgage market. Why make a proposal that would benefit all except the borrowers who most need it?

Second, we recommend against including an interest rate in the GMP. Including it in a "guaranteed mortgage package" and calling it a "guaranteed rate" (even with qualifications) would lead to terrible misunderstandings. It is simply not guaranteed. The reason it is not guaranteed is because (1) it is expected to float, unless locked in by the consumer; and (2) it is provided too early in the loan shopping process to be reliable.

Many lenders report that the information they have at the early date when the inquiry is taken is not accurate enough—particularly about the price of the property—to give any certainty about the rate they can offer the consumer. Therefore, even if the consumer is able to track the rate between the application and closing, the consumer cannot know with any confidence that the rate will not change for reasons that can only be known to the lender. Because the disclosure must be given before an application is taken and before any fee is paid, the loan has not been underwritten and the rate will often be subject to change, as the lender obtains a property appraisal and more thoroughly underwrites the loan. Although we recognize that the rate is a valuable disclosure for the consumer to receive, and can be useful when the consumer shops for credit, it is inappropriate as part of the GMP.

Third, we would oppose any approach that called for lenders to adjust their rates based only on an external index (such as LIBOR). The pricing of products is a proprietary business, and each lender does it in its own way based on many factors, including the fluctuations in the secondary market, the need to hedge, the desire to attract customers to certain products, and so forth. But there is no reason for the lender to rely exclusively on some external index. If HUD were to impose such a requirement, it would dramatically change the economics of mortgage lending and the pricing of mortgage loans, in ways that we cannot yet determine. Ultimately, we believe it would create a safety and soundness concern for lenders and could drive up the cost of credit for consumers.

Under the proposal, lenders who do not wish to offer GMPs could continue to provide the Good Faith Estimate of Closing Costs (GFE)—but HUD is proposing significant changes here as well. The GFE would be grouped differently by categories, and, although it would continue to comprise estimates of settlement costs, the estimates would be required to be accurate—or in some cases within a 10% tolerance. Lenders who choose the enhanced GFE option would not get the benefit of a safe harbor from section 8 of RESPA. Under the GFE Option, mortgage brokers would also provide a new disclosure that explains their role in the transaction. Yield spread premiums would be disclosed on the GFE as an amount paid by the lender to the borrower. This is intended to ensure that borrowers receive the full benefit of a higher price paid by wholesale lenders for a loan with an above-par interest rate.

We support improved disclosure of broker's fees, but HUD's proposed approach appears more likely to confuse consumers. There are better alternatives. If the goal is to clarify the treatment of broker fees and the relationship of the parties, we recommend employing something akin to the Broker Disclosure Fee Agreement, previously recommended by many in the industry.

Beyond new disclosures of mortgage broker fees, however, changes to the GFE ought to be deferred at this time. The new GMP option is more than enough for lenders and consumers to absorb, without making dramatic changes to the status quo at the same time. As HUD conceives the proposal, lenders would be forced to choose between two significant changes in the way they do business. In our comments, we urged HUD to wait until the GMP option has been introduced and had a chance to be accepted. Until then, we will not have a good understanding of what changes to the GFE, if any, are necessary.

We have many other comments regarding HUD's proposal, which we address in greater detail in our comment letter to the agency. In general, however, we remain committed to the idea of reform, and will be happy to work with the agency and this subcommittee toward that end.

Thank you again for the opportunity to share our views.

October 28, 2002

Rules Docket Clerk
Office of General Counsel, Room 10276
Department of Housing and Urban Development
451 Seventh Street, SW.
Washington, DC 20410-0500

RE: Docket No. (FR-4727-P-01); Proposed Rule on Real Estate Settlement Procedures Act (RESPA)

To the Office of General Counsel:

The Consumer Bankers Association (CBA)[1] is submitting this letter in response to the Department of Housing and Urban Development's (HUD) request for comment on a proposal to modify its Regulation X, which implements the Real Estate Settlement Procedures Act (RESPA). This proposal (Proposal) intends to simplify and improve the process of obtaining home mortgages and reduce settlement costs for consumers. It includes provisions for a new Guaranteed Mortgage Package (GMP) and revises the Good Faith Estimate (GFE) to assist consumers in shopping and comparing costs in home mortgage transactions.

The Proposal would create two parallel approaches to offering closed-end mortgage loans—both considerably different than the current scheme—that could be employed at the option of the originator.

Under one option, lenders would offer, at no cost to the consumer, a guaranteed package price to anyone who inquired about a loan and provided certain basic information. The offer, called a "guaranteed mortgage package", would have to be provided within 3 days of the inquiry, and must be kept open for 30 days.

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[1] The Consumer Bankers Association is the recognized voice on retail banking issues in the nation's capital. Member institutions are the leaders in consumer financial services, including auto finance, home equity lending, card products, education loans, small business services, community development, investments, deposits and delivery. CBA was founded in 1919 and provides leadership, education, research and federal representation on retail banking issues such as privacy, fair lending, and consumer protection legislation/regulation. CBA members include most of the nation's largest bank holding companies as well as regional and super community banks that collectively hold two-thirds of the industry's total assets.

A GMP would include (1) an early interest rate disclosure that the consumer could keep track of prior to lock in (called a "guaranteed" interest rate), and (2) a guaranteed lump-sum amount of settlement costs (including all lender required settlement services except per diem interest, hazard insurance, and escrow/reserves). Some additional TILA-type disclosures (including the APR) would be provided as well.

Those lenders who offer a GMP would be entitled to an exemption from RESPA's section 8 prohibitions on referral fees for settlement service costs within the GMP package. If the customer accepts the offer, the lender would be contractually bound not to charge more than the GMP Agreement (GMPA).

HUD believes that the GMPA concept will be an appealing option for many lenders, since it will permit them to negotiate packages at favorable costs. Consumers will benefit because the market forces will drive down the prices of settlement services, and because they will be provided a "guaranteed" price upon which to shop for the best terms. However, this GMP option would not be available to consumers obtaining HOEPA loans.

Under the Proposal, lenders who do not wish to offer GMPs could continue to provide the Good Faith Estimate of Closing Costs (GFE)—but HUD is proposing significant changes here as well. The GFE would be grouped differently by categories, and, although it would continue to comprise estimates of settlement costs, the estimates would be required to be accurate—or in some cases within a 10% tolerance. (Under the current GFE, there is no requirement that the final costs be the same as the GFE, and generally no liability if they are inaccurate.) The APR and other TILA disclosures would be given with the GFE as well. Lenders who choose the enhanced GFE option would not get the benefit of a safe harbor from section 8 of RESPA.

Under the GFE Option, mortgage brokers would also provide a new disclosure that explains their role in the transaction. Yield spread premiums would be disclosed on the GFE as an amount paid by the lender to the borrower. This is intended to ensure that borrowers receive the full benefit of a higher price paid by wholesale lenders for a loan with an above-par interest rate.

We greatly appreciate the opportunity to comment on the Proposal and we look forward to working with HUD in the future as final changes are made to Regulation X.

CBA Comments

CBA has for years been actively engaged in the discussions about RESPA/TILA Reform. We have long endorsed a position that would permit lenders to offer some guaranteed settlement service cost package, with section 8 exemption. Therefore, we strongly support HUD's initiative.

However, there are many details to be worked out, since this calls for a significant change in the mortgage and home equity lending businesses.

Because of the difficulty of presenting our comments as responses to the questions posed, we have chosen to offer our comments in a different format, but indicate, when such is the case, the questions upon which they bear.

I. CBA is supportive of the concept of a guaranteed settlement cost package in return for a safe harbor from section 8 of RESPA.

First and foremost, we wish to indicate our support for HUD's overall efforts. We have long been active in the efforts on the part of the industry, consumer groups and the regulatory agencies to solve the problem of the complex regulatory regime to which mortgage lending is subject.

When a 1996 statutory requirement[2] called for the Federal Reserve Board (FRB) and HUD to recommend ways to simplify and improve the disclosures required by the Truth in Lending Act (TILA) and the Real Estate Settlement Procedures Act (RESPA), we participated in regular discussions between industry and consumer organizations to seek workable solutions that might be proposed to the agencies. The group that met, loosely known as the Mortgage Reform Working Group (MRWG), although unable to reach a formal consensus of opinion, brought forth ideas that were the direct precursor to HUD's Proposal—including the concept of an optional guaranteed settlement services package in lieu of the GFE. Ultimately, the idea was endorsed by both agencies in the HUD/FRB Report to Congress on the reform RESPA and TILA.

We were early supporters of the idea, because we believed it would have multiple advantages: It would reduce the complexity of disclosures; it would provide useful shopping information at a more advantageous time for the consumer; it would allow market forces to keep costs down; and it would reduce the likelihood that the consumer would be surprised by the dollar amount needed at the settlement table. In order to make the guaranteed package work, HUD would need to exempt the elements of the package from the restrictions of Section 8 of RESPA; otherwise, lenders would avoid packaging out of concern about liability risk. In our testimony to Congress on September 16, 1998, we stated: "We support the idea of guaranteed closing cost packages coupled with section 8 relief because we believe there may be potential marketing benefits to lenders, increased simplicity of disclosures, and cost savings to consumers."

However, we believe it is incorrect and potentially misleading to call it a Guaranteed Mortgage Package or to state that the interest rate is part of the guarantee. By using this term and including references to a guaranteed rate, HUD is putting lenders (and other packagers) in the position of implying that they are offering a loan commitment. We recommend the use of a phrase that more accurately reflects

[2] Section 2101 of the Economic Growth and Regulatory Paperwork Reduction Act of 1996.

the situation, such as Guaranteed Settlement Cost Package. As noted below, we also suggest that the interest rate should be removed from the package; or that the package more clearly state the qualified nature of the rate disclosure.

II. HUD should defer any changes to the existing GFE system (except regarding the treatment of broker fees), while the new GMP is introduced.

We recommend deferring changes to the GFE until a later date, when a more informed decision can be made about what changes are appropriate and what is within HUD's legal authority to accomplish. HUD's proposal creates a dramatic change in the way mortgage lending will be done in this country for the foreseeable future. The bold concept of a GMP, permitting consumers to shop more easily for mortgage credit will change the face of lending, putting everyone whose business touches on mortgages in a new world, requiring new systems, training, and forms. But even more significantly, the introduction of the GMP option will force a realignment of business and a reassessment of pricing that we cannot really foresee at this time. These are changes that need to be entered into with care. The fact that HUD is presenting them as an option suggests a recognition of the need to allow lenders and other service providers to come into this in their own way.

Yet introducing changes in the GFE at the same time would make it more of a false option. There would be no *status quo*. Lenders would have to choose between one significant change and another. Many lenders are also quite wary of the GMP option. They wish to take a wait and see approach. We believe it will be successful and beneficial to consumers and industry alike; but it is an experiment that must be allowed a fair chance to work. Lenders will come around to it given an opportunity. Right now, their support for the Proposal may depend on their not believing that they are being railroaded into making changes.

Even the imposition of tolerances on the GFE would be an unacceptable change at this time. Although it may not be apparent on the face of it, numerical tolerances will call for significant changes in the behavior of lenders and brokers. They would operate as a kind of quasi-guaranty, that would force lenders and brokers to factor changes into their pricing structure, to explain changes that are due to unforeseen circumstances, and to run the risk of harming customer relations. Indeed, there would be little reason to choose the GFE option, since the tolerances force lenders to essentially guarantee the settlement service costs, but without the benefit of the section 8 exemption.

2. Treatment of broker fees. Regarding the treatment of mortgage broker fees (such as "yield spread premium"), the Proposal would require that any payments from a lender based on a borrower's transaction, other than a payment to the broker for the par value of the loan, including payments based upon an above par interest rate on the loan, *be reported on the GFE and HUD-1 as a lender payment to the borrower*. The approach suggested in the Proposal has the advantage of simplicity; but we believe it is outweighed

by the potential for confusion. We are concerned that consumers will not understand the nature of the disclosure.

If the goal is to clarify the treatment of broker fees and the relationship of the parties, we recommend, in the alternative, requiring brokers to offer a disclosure such as the Broker Disclosure Fee Agreement, previously recommended by many in the industry. A copy of the form that was recommended by a number of trade groups is attached as an addendum to this comment letter. Should this approach be taken, we would recommend that it be republished prior to final issuance, so that everyone affected can have an opportunity to comment.

III. Interest rate should be separated from guaranteed settlement service package and –if disclosed—more accurately described as conditional

We have serious reservations about the inclusion of the interest rate in the GMP. Including it in the package, and calling it a guaranteed rate, will lead to terrible misunderstandings. It is simply not guaranteed. The reason it is not guaranteed is because (1) it is expected to float, unless locked in by the consumer; and (2) it is provided too early in the loan shopping process to be reliable. Although we recognize that the rate is a valuable disclosure for the consumer to receive, and can be useful when the consumer shops for credit, it is inappropriate as part of the GMP.

The fact that the rate can float between the time of the disclosure and the closing (unless it is locked) is reason enough to avoid calling it a guaranteed rate. But as an added concern, many lenders report that the information they have at the early date when the inquiry is taken is not accurate enough—particularly about the price of the property—to give any certainty about the rate they can offer the consumer. Therefore, even if the consumer is able to track the rate between the application and closing, the consumer cannot know with any confidence that the rate will not change for reasons that can only be known to the lender. Because the disclosure must be given so early in the "application" (really before an application is taken) and before any fee is paid, the loan has not been underwritten and the rate will often be subject to change, as the lender obtains a property appraisal and more thoroughly underwrites the loan.

The GMPA states, in the introductory paragraph, "This Agreement is subject to verification of your credit rating, final property appraisal, and other appropriate underwriting criteria." But this phrase is hidden in a document that otherwise states, on numerous occasions that the rate is guaranteed. For example, all of Paragraph I is called, in bold-face type, an "**Interest Rate Guarantee**." The same paragraph states, "…we guarantee that the interest rate will not exceed __% [over][under] the [prime][index] rate for __ days [30 days or greater]." The entire document, which includes the rate disclosure, is called a "Guaranteed Mortgage Package Agreement." While the ability of the rate to float is explained, it does not adequately explain the many ways in which the price of the property, the consumer's credit history, and the other factors that play into risk-based pricing may effect the cost of the credit, and the "subject to" language is totally inadequate to counter the impression that the form will leave the consumer.

Misunderstandings are a virtual certainty. Consumers who are aggrieved will blame the lenders, resulting in bad customer relations and significantly increased litigation risk. Inevitably the cost of credit will rise, as lenders seek to protect themselves against the risk of understatement and cover the increased costs of "guaranteeing" a rate.

Clearly HUD contemplated the problems that might arise if lenders were forced to guarantee rates, and proposed, in the alternative, that there be some mechanism in place that would permit the rates to float, while allowing consumers to track their rate. The ability to track the rate is designed to protect the consumer from rate manipulation by unscrupulous lenders. Two possible approaches to this have been suggested. One would force lenders to identify an external index to which they would tie their rates, and the other would call for lenders to make their rate changes known according to a publication that can be monitored by the applicant. We believe that neither would be workable.

We would strongly oppose any approach that called for lenders to adjust their rates based only on an external index (such as LIBOR). The pricing of products is a proprietary business, and each lender does it in its own way based on many factors, including the fluctuations in the secondary market, the need to hedge, the desire to attract customers to certain products, and so forth. But there is no reason for the lender to rely exclusively on some external index. If HUD were to impose such a requirement, it would dramatically change the economics of mortgage lending and the pricing of mortgage loans, in ways that we cannot yet determine.

Ultimately, we believe it would create a safety and soundness concern for lenders *and could drive up the cost of credit for consumers.* If lenders are required to guarantee interest rates within three days after receipt of an application and are only permitted to change the rate because of an increase in the cost of funds (i.e., as measured by outside index movements), risk-based pricing may no longer be possible, resulting in very significant changes in the way housing financed is priced today. These changes are more than likely to result in higher interest rates to borrowers as a lender hedge against the forced absence of pricing flexibility and the inability to price according to risk.

Certainly permitting the use of the lender's published rates (such as posted rates on the lender's web site) is preferable to mandating the use of external indices, but this approach is problematic as well. If, due to the subsequent underwriting, some consumers cannot be offered the precise rate they were initially disclosed, *they would be mistakenly following the wrong rate on the lender's chart.* Other complications can also interfere with the consumer's ability to track the rate changes. One common one might be if the consumer wishes to add or subtract discount points from his or her original application—something consumers routinely do. Discount points are almost formulaic in their relationship to the rate, but most consumers would still require an elaborate rate spread sheet to see what happens to each rate based on changes in the amount of the discount points.

We recommend that several steps be taken to address these concerns. **First, as noted above, to prevent problems between consumers and packagers or lenders, we recommend that the term "Guaranteed Mortgage Package" be eliminated.** The entire package, after all, is not guaranteed. Instead, it should be called a Guaranteed Settlement Cost Package (or something similar).

Second, we recommend that the interest rate should be eliminated from the package. Rates would continue to be handled the same as they are currently; i.e. disclosed according to Regulation Z and floating unless locked in by the consumer after paying a lock-in fee.

If the interest rate does remain, however, we believe the disclosure should <u>clearly state</u>, in large type, easy to understand, that the rate is NOT guaranteed, and that it IS SUBJECT TO CHANGE.

If the rate is not locked, it is essential that it be permitted to float according to whatever mechanism is most appropriate to that lender's pricing, and not according to some index outside of the lender's control.

<u>IV. APR and other TILA disclosures should be excluded from the reform package.</u>

All the TILA requirements, including the APR, are inappropriate for inclusion in the RESPA disclosures. If one of the goals of this reform effort is "to simplify...the mortgage loan process," as HUD has stated, this would do just the opposite. All the TILA disclosures are redundant and would only complicate the mortgage disclosure process.

In particular, requiring the inclusion of the APR in the early RESPA forms raises a number of serious problems. The APR is a figure that is defined with great precision by the Federal Reserve Board. HUD's definition would need to track the Federal Reserve Board's or risk confusion. Yet, because RESPA's timing precedes TILA's, lenders (or other packagers) would need to provide the APR before enough information is available to provide for an accurate figure. For example, an accurate APR cannot be provided at the early time required by RESPA, without knowing whether mortgage insurance will be included in the loan. HUD should avoid confusing the two regulations.

<u>V. HOEPA loans should not be excluded from the GMP Option.</u>

HUD, with little supporting commentary, has proposed excluding HOEPA loans from the GMP option. We do not agree.

HUD's Question 15 states: "As proposed in Section III.C(6), under the rule, mortgages with total fees or a rate covered by the Home Ownership and Equity Protection Act (HOEPA) would be subject to the new GFE disclosure requirements; however, HOEPA loans would not qualify for the guaranteed package safe harbor. Is this exclusion appropriate considering, on the one hand, that packaging promises borrowers a simpler way to shop and make transactions more transparent? On the other hand, the safe harbor could be provided for a loan that has very high rate and/or fees and may be predatory. The proposal also says that during the rulemaking other limitations may be established to exclude high cost and/or loans with predatory features from the packaging provisions. HUD invites comments on whether HOEPA loans, any other loans, or features of loans should be included or excluded from the safe harbor and why." 67 FR 49156.

We are strong proponents of legitimate efforts to prevent abusive lending practices, and we agree with most thoughtful observers that one of the best antidotes to predatory lending is a competitive market and an informed consumer. We can understand HUD's reluctance to extend the protections of the GMP to high cost loans that might be predatory. But HOEPA loans are not, by virtue of being subject to HOEPA, predatory. They merely have costs that are higher than average and that trigger the HOEPA requirements. HOEPA's requirements are imposed precisely in order to reduce the likelihood that they will be abusive. It is often said that consumers who are in the subprime market do not shop for credit. We believe that they fail to shop in part because the existing mortgage lending process makes it so difficult to do so, and aids the unscrupulous lender, broker or service provider in imposing unreasonable terms and conditions on their customers. The Proposal is an effort to remedy this by providing by simplifying and clarifying the disclosures of the costs of lending, and enhancing the opportunity for consumers to shop for the best mortgage and refinancing.

As Secretary Martinez noted in his testimony before the U.S. House Financial Services Committee, October 3, 2002, "Injecting greater competition into the mortgage lending process and among settlement services is an important reason for reforming RESPA. When consumers are empowered to shop for the best loan to meet their needs, the market will respond to the competition by lowering costs. When closing costs are reduced, home loans will become less expensive and more families will become homeowners."

The Secretary also stated, "We believe that our proposed reforms, and the greater transparency they ensure, will make it more difficult for unscrupulous lenders to abuse borrowers." HUD is sending a mixed message if it withholds these benefits from the very consumers who need them most. If HOEPA lenders cannot take advantage of it, there will be a two-tiered lending world, with some consumers paying more, because HUD will not permit them to take advantage of the competitive market.

From an operational perspective, there is another reason not to exclude HOEPA loans from the GMP. The GMP is provided so early in the application (or inquiry) process, that lenders cannot know with any degree of certainty if the loan will prove to be subject to HOEPA. They could start by assuming that, based on the information provided, the loan is not a HOEPA loan and offer a GMP, only to discover after subsequent underwriting that the GMP should never have been provided. The inability for lenders to know, early enough in the application process, whether the consumer is going to only qualify for a HOEPA loan, will make it difficult for lenders who even *offer* HOEPA loans ever to use the GMP option.[3]

VI. Issues of compatibility with other federal laws must be resolved.

Inconsistencies with FRB-issued regulations, such as Z, B and C must be carefully resolved. Although they may appear to be small matters in the overall scheme, these inconsistencies could undermine the effort to reform RESPA by making the use of the GMP, for example, so difficult as to be undesirable. We do not have solutions to all these problems, but we urge you to put your resources to work, jointly with the Federal Reserve Board where necessary, to minimize these problems. Those that have come to light are the following:

A. Regulation Z. Use of the GMP and revised HUD-1 can result in Regulation Z compliance problems. This is caused specifically by the elimination of an itemized list of prepaid charges, which are currently required in the GFE and HUD-1. Under the Proposal, lenders cannot know which components of the prepaid items are prepaid finance charges under TILA and which are not. In addition, those lenders who need to determine whether their loans meet the HOEPA threshold will be unable to do so without being able to itemize the components that apply to the threshold determination and the components that do not.

Even if the prepaid charges needed to compute the finance charge for TILA are itemized with the HUD-1 when lenders employ the GMP,[4] problems arise. Lenders cannot itemize individual charges if the amounts of the various services have been negotiated as a package. Inevitably, they will be challenged on the amounts that they attribute to each individual transaction. Furthermore, the information at closing is offered too late to be entirely helpful. TILA requires early disclosures to be given for purchase money mortgages, but lenders will not have the complete breakdown of charges needed to calculate the APR accurately.

[3] Generally speaking, we recommend that GMP should be available as widely as possible. As a purely technical matter, it is useful for lenders not to have to distinguish between covered loans and those that are not. Since the GMP is entirely optional, allowing it to be employed does not require lenders to use it for any particular product or loan.

[4] The Proposal states, "[B]ecause the amounts of certain individual charges needed to compute the finance charge and the APR under TILA and HOEPA [sic], the packager must list the finance charges needed to calculate the APR on an addendum to the HUD-1 or HUD-1A." 67 FR at 49153.

If HOEPA loans are not given the safe harbor from section 8 under the GMP option (as HUD has proposed), lenders will want to avoid offering the GMP on HOEPA loans. However, because they will not have an accurate breakdown of the charges that apply to the threshold under HOEPA, they will need to err on the high side and avoid offering the GMP to any loan that is even close to being covered by HOEPA.

If, instead, lenders are told to include the full amount of all prepaids as if they are covered by TILA and apply toward the HOEPA threshold, the result will raise APRs (and, incidentally, increase the number of HOEPA loans) for all loans that are subject to RESPA. Of course, the same will not be true of loans that are not subject to RESPA (e.g. home equity loans)—making APRs not comparable between different products.

Timing concerns also arise in regard to Regulation Z. The new timing requirements of the Proposal, i.e. within three days of the "application," as that is defined by the Proposal, is earlier than the Regulation Z timing, as well. Even though early TILA disclosures are required for purchase money mortgages, they are not required for refinancings, which are subject to RESPA. In addition, the early disclosures are not required to be given until three business days after receipt of a "written application." The Proposal would require the GFE or GMP to be provided at an even earlier time, and it is even triggered by an oral inquiry that has the requisite elements.

We urge HUD to resolve these incompatibilities and inconsistencies with Regulation Z by opening a dialogue with the Federal Reserve Board and seeking a solution that is simple and practical for lenders and packagers, and informative for the consumer.

B. "Application." The definition of "application" raises concerns that go to the treatment of loans under Regulation B (ECOA), Regulation C (HMDA). Definitions of applications vary among these regulations, with varying consequences for the lender and consumer. By creating a new definition that is earlier than all the others, HUD is sowing confusion. Under the Proposal, the definition of "application" would be changed to be "whenever a prospective borrower provides a loan originator sufficient information…, whether verbally, in writing or computer generated, to enable the loan originator to make a preliminary credit decision concerning the borrower… ." According the Proposal, sufficient information is "typically a social security number, a property address, basic employment information, the borrower's estimate on the value of the property, and the mortgage loan needed." 67 FR at 49149. These five items alone, particularly if they are taken over the phone, are not usually enough to amount to an application under the other regulations. These are the elements of an inquiry, not an application. Yet by calling the event an application, HUD raises a number of possible concerns: e.g. does a denial of a RESPA application amount to a denial of an application under Regulation C? What is the impact on HMDA reporting? Would the prospective borrower making an inquiry under RESPA that must be treated as an "application" be an "applicant" under Regulation B?

We believe the answers to all these questions are the same: that a RESPA application, as defined by the Proposal, is not an application at all, and would not have any consequences under these other regulations. **We would urge HUD to avoid confusion by changing the name of the event. Calling it a "pricing inquiry," or a similar phrase would also be more descriptive and understandable to the consumer.** As a statutory matter, this would merely give the same event a new and more descriptive name.

C. Bank Holding Company Act. One critical concern for banks is the relationship of the Proposal to the Bank Holding Company Act (BHC Act). Section 106 of the BHC Act Amendments of 1970 creates potential conflicts for banks using the GMP option. The tie-in rules prohibit banks from requiring the use of an affiliated service provider. This might raise concerns for banks who have affiliated service providers that might be included in a GMP offered by them or by a third party, or who decline to approve a package that may include a service provider affiliated with a competitor; and a differentiation between BHC's and others could result in an uncompetitive environment.

It is important for HUD to work with the Federal Reserve Board to clarify how banks can employ the GMP without running afoul of the BHCA and other banking statutes and regulations.

VII. HUD must explicitly preempt state laws that would conflict with compliance.

Preemption of certain state laws will be necessary if the GMP option is to prove successful. A number of situations may arise that call for preemption of state laws, among others, including:

*State disclosure laws, including laws regarding the itemization of certain charges
*State laws requiring borrower choice of service providers
*State anti-affiliation laws and tie-in restrictions
*State kickback and anti-referral fee laws (mini-RESPA laws)
*State laws requiring the separate disclosure of yield spread premiums

RESPA preempts state laws "to the extent that those laws [concerning settlement practices] are inconsistent with any provision of this Act, and then only to the extent of the inconsistency." Moreover, HUD may not determine that a state law is inconsistent if it affords consumers greater protection than RESPA provides. Section 8(d)(6) of RESPA states, "No provision of State law or regulation that imposes more stringent limitations on affiliated business arrangements shall be construed as being inconsistent with this section."

We recommend that HUD make an express finding in its final rule that all such laws, and any others that it may identify as problematic, are in conflict with the revisions to RESPA, since they frustrate its purpose and provide less consumer protection. It should further determine that the final rule regarding the GMP is more protective of consumers and competition in the marketplace.

VIII. Technical violations of RESPA should not cause excessive liability.

Under the GMP option, any small error in disclosures (including the TILA disclosures, which we have elsewhere recommended to be eliminated from the package) or in the timing or other technical requirements could result in the loss of the safe harbor from section 8. This would be inappropriately severe repercussion. We believe the safe harbor exemption should be available to packagers and service providers as long as the guaranteed settlement cost figure is accurate.

Furthermore, the loss of the safe harbor exemption on one loan runs the risk of significant liability if the safe harbor –involving negotiations for services involving multiple transactions—is threatened. To address this concern, we believe there should be an opportunity to cure honest mistakes without losing the exemption. Permitting a lender to refund an error to cure a good faith error would protect consumers without unduly harsh penalties on lenders and service providers.

IX. Considerable time will be needed for the industry to implement the changes.

We are recommending against most mandated changes to the GFE process. The GMP is entirely optional. We therefore recommend that any mandatory changes that are adopted be given as long as **two years** for lenders to implement. Lenders who are HMDA reporters already have costly and time-consuming implementation requirements between now and January 2004.

Additional Issues

A. Regulation of costs.
The regulation does not permit packagers to charge for the cost of providing the package offer (notwithstanding the fact that lenders can charge a nominal amount when providing a GFE). Subsequently, the prospective borrower can be charged a "minimal" fee when the offer is accepted. We recommend that the packager be permitted to charge the consumer at the time the of the GMP offer, in order to cover the cost of providing the offer. Subsequent charges should not be limited by HUD at all.

We understand that it is HUD's intention to create an environment conducive to shopping, where the prospective borrower has no investment in the transaction before selecting a package or a lender. However, the mortgage lending process is not a matter of choosing an item off a shelf. Someone has to pay for the time and effort that goes into providing the price quote. Ultimately, if the shopper does not cover that cost, it will be passed on to the smaller number of those who do obtain a loan, driving up their cost of credit.

B. The GMP should exclude certain items.
Although we agree that it is useful to have only a limited number of figures to compare when an applicant is shopping for credit, some of the amounts that are included in the GMP are likely to throw it off dramatically if they are wrong and may be too difficult to provide with sufficient degree of accuracy. The concept of a "guarantee" would be totally undermined if these amounts must be included in the GMP, and consumers would be misled.

We recommend the exclusion of the following items from the package. In addition, we recommend the exclusion of costs that are not relevant to the consumer's decision when shopping for credit, that arise from a consumer's change or subsequent request, or that are to satisfy closing conditions rather than to pay for settlement services.

- **Mortgage insurance premiums (MIP).** Although the amount of MIP is to be specifically identified, along with a disclosure that it is subject to change[5], it is still to be included in the total GMP cost figure. Until the appraisal, even whether MIP is needed is not known for sure. If that figure is wrong, it will result in a significant inaccuracy in the total GMP disclosure. We therefore recommend that the GMP price not include mortgage insurance.

- **Discount points.** Discount points are not settlement services at all, but are related to the price of the loan itself. They do not belong in a package of settlement service fees. Borrowers choose to pay points to reduce the rate. Thus, the amount of the points is tied to the rate, and borrowers can make changes after the application as their needs or desires change. As borrowers may often want to change the relationship of the points to the rate during the application process, the changes should not affect the settlement cost figure.

- **Rate lock fees.** HUD should clarify that that rate lock fees are excluded from the package. A separate location for disclosing rate lock fees is required.

- **Flood insurance.** Flood insurance is a service that may not be required to be purchased, depending upon whether or not the property is located in a flood zone, as indicated by the flood search report. The flood search will not be ordered or performed until the applicant accepts the package. Thus, the lender will not know

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[5] Mortgage Insurance disclosure needs to reflect potential <u>increase</u> as well as decrease. GMP also includes up-front costs of mortgage insurance, based on the ratio of the loan amount to the value of the property. Since the lender does not have the value of the property with certainty at the time of the disclosure—within 3 days of the initial inquiry—the lender must estimate. According to HUD, the disclosure should reflect the "maximum" possible insurance, and include a disclosure that the amount of mortgage insurance premium "may decrease or become unnecessary" depending on the appraisal. However, the possibility exists that the potential borrower will overestimate the value of the property—resulting in an under-disclosure of the MI, or the mistaken impression that MI is unnecessary. It is important that the disclosure clearly reflect that fact.

whether flood insurance will be required or how much the insurance will cost until the lender receives this report.

- **Charges payable in a comparable cash transaction.** We recommend that the GMP cost amount not include any charge payable in a comparable cash transaction. Thus, while mortgage recording taxes and charges are in the GMP cost amount, transfer taxes paid on the recorded deed in a purchase transaction or property taxes that are apportioned in a purchase transaction should not be. This is consistent with TILA's definition of a finance charge. Under TILA, finance charges exclude any charge "of a type payable in a comparable cash transaction."

C. GMP offer should not have to be open for 30 days from when the document is delivered or mailed to the borrower.

We recommend shortening the time frame for keeping offers open. Thirty days is an unnecessarily long time if the purpose is to permit shopping. While some may take that long to shop for a loan, those who are serious should be able to do so in much less time. Further, the requirement to maintain the offer for 30 days could increase the cost of credit. **We recommend 10 days as the maximum needed for the offer.**

D. HUD should explicitly state that packaging is a primary market activity.

The Proposal states that a packager is any person or other entity that offers and provides GMPs to borrowers. Proposed § 3500.16(b). The Proposal, however, should clarify that packaging is a primary market function, not open to entities whose charter prevents them from primary mortgage market activities.

E. The requirement to provide copies of certain documents (e.g. pest inspection; appraisal; credit report, and lender's title) to consumer on request is unnecessary.

These are new requirements, which will only add to the burden and complexity of the new rules. The pest inspection is done for the benefit of the lender, as is lender's title. The other two documents, appraisal and credit report, are already required to be provided to consumers under other laws.

In regard to Credit Reports, the Fair Credit Reporting Act already gives consumers a right to a free copy of their credit reports, directly from the credit bureau, in certain instances such as when the consumer has been denied credit. Some credit bureaus, as a condition of doing business, require lenders to agree not to directly provide consumers with credit report copies. Also, releasing third-party account experience may arguably make a lender a "credit reporting agency" under the Fair Credit Reporting Act. In the absence of a federal law clearly mandating and authorizing lenders to provide credit report copies to consumers, we ask that HUD not require lenders to offer credit report copies.

Regarding the lender's title policy, it would be extremely misleading to provide a copy to the borrower. Borrowers may take this as an implication that they have some protection or right to rely on the lender's title policy, which is not the case.

The borrower already has a right to a copy of the appraisal under the ECOA and Regulation B. An additional requirement under RESPA is unnecessary and redundant.

F. Clarification of Safe Harbor.
HUD should clarify that the arrangements covered by the GMP safe harbor exemption may not be used to challenge referrals to service providers in connection with loans not covered by the exemption, if the arrangements are separately negotiated and by their terms apply only to referrals made for loans covered by the exemption.

Thank you for your consideration in these matters. If you wish any further information, please do not hesitate to contact me.

Very truly yours,
S/

Steven I. Zeisel
Senior Counsel

Attachment

Mortgage Broker Fee Agreement

In the following: "I" or "me" = applicant; "You" = mortgage broker

Mortgage Broker Service. You are duly authorized and prepared to assist me in arranging mortgage financing for my home, and you agree to provide such assistance, as set forth below.

Amount of Broker Compensation. I understand that, as compensation for the goods, services and facilities you provide, your total mortgage broker compensation from all sources will not exceed:

[$_________________]

and / or [*specify which*]

[__________________ point(s)] (one point equals 1 percent of the original principal balance of the actual mortgage loan obtained).

Method of Broker Compensation Payment. I understand that I may have a choice as to how your compensation is paid. Depending on such factors as my financial circumstances, whether I qualify for a loan and/or whether a loan program is available:

- I may pay your compensation for the services you provide out of my pocket directly.
- If I want to lower the amount I compensate you out of my pocket directly:

  → I may have the lender pay some or all of your compensation, in which case the lender will charge me a higher interest rate which could result in higher monthly payments; and/or

  → I may use the proceeds of the loan to pay some or all of your compensation, in which case I will be obligated to repay that amount with interest over the term of the loan.

I understand that I should discuss with you in further detail the specific options available to me to pay for your compensation, including the impact of each such option on the amount of cash I must bring to the closing, my interest rate, loan amount and monthly payments.

Nature of the Relationship. [Choose appropriate text][standard][I understand that in connection with this Agreement, you are not acting as my agent. You are also not acting as the lender's agent. Although you seek to assist me in meeting my financial needs, you may not make available the products of all lenders or investors in the market or the lowest prices or best terms available in the market.]

[California/FHA][I understand that in connection with this Agreement and any mortgage loan you arrange for me, you are acting as my agent. You are not acting as the lender's agent. Although you seek to assist me in meeting my financial needs, you do not distribute the products of all lenders or investors in the market and cannot guarantee the lowest price or best terms available in the market.]

[lender's agent] In assisting to arrange financing for my home, I understand that you are not my agent and that you are acting as the agent of the lender.]

Termination. This Agreement will continue until one of the following events occurs:

- I fail to receive loan approval;
- My loan closes;
- I terminate this Agreement;
- You and I enter into a new Mortgage Broker Fee Agreement; or
- ____________ days expire from the date of this Agreement without any of the foregoing occurring.

Mortgage Broker Fee and Disclosure Acknowledgement

By signing below, I/we understand and agree to the terms of this Agreement. The contractual obligation to comply with this Agreement rests solely with the mortgage broker and the applicants signing below. No other entity shall be liable for any misrepresentation or non-performance of the mortgage broker's obligations under this Agreement, or the mortgage broker's collection of compensation in excess of the maximum compensation amount stated herein.

Signing this Agreement does not obligate me to obtain a mortgage loan through you, nor does it prevent me from shopping for mortgage loans with any other mortgage broker or lender. This Agreement does not constitute a loan commitment or otherwise indicate mortgage loan approval.

I acknowledge that you and any lender that makes a loan to me is relying upon this Agreement and upon my statement that I actually understand your role in the transaction and how you will be paid.

* * Applicant______________________ Date__________________

* * Applicant______________________ Date__________________

____
Mortgage Broker's Signature
Mortgage Broker's License No. (where applicable) ________________________

INDEPENDENT COMMUNITY BANKERS OF AMERICA

BEFORE THE

HOUSE FINANCIAL SERVICES HOUSING SUBCOMMITTEE
U.S. HOUSE OF REPRESENTATIVES

FEBRUARY 25, 2003

The Independent Community Bankers of America (ICBA)[1] is pleased to submit written testimony today on behalf of our nearly 5,000 community bank members, and to share with you their views on the Department of Housing and Urban Development's (HUD) proposed Real Estate Settlement Procedures Act (RESPA) rule. On October 28, 2002, ICBA responded to the invitation to comment on the proposed rule, and submitted an extensive letter to HUD, a copy of which is attached for your reference.

ICBA and its members place a high value on the importance of homeownership. Our current mortgage finance system has enabled a record number of Americans to realize that dream, and we fully support the administration's goal to further increase minority homeownership by 5.5 million families. It is a simple fact that the lower the costs of obtaining a mortgage, the more affordable homeownership becomes.

HUD's proposed rule has been presented as an attempt to simplify and improve the process of shopping for mortgage loans with the three main objectives being to: (1) fundamentally change the way in which mortgage broker compensation is reported; (2) improve the existing RESPA disclosure scheme; and (3) remove regulatory barriers to enable the offering of packages of settlement services to borrowers.

While the ICBA is a proponent of simplifying the mortgage loan process, and giving borrowers more choices, we have serious concerns with the proposed rule, because it will seriously undermine the mortgage finance process, and reverse the trend of overall homeownership growth. We firmly believe that should this rule be adopted as it stands, it will, at a minimum, result in borrower confusion, hidden fees, increased settlement costs, and fewer credit and settlement service options as small lenders and brokers are driven from the market because they simply will not be able to negotiate the necessary discounts from settlement service providers to compete with larger institutions -- in short, a serious disruption of the mortgage finance system.

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[1] ICBA is the primary voice for the nation's community banks, representing nearly 5,000 institutions with 17,000 locations nationwide. Community banks are independently owned and operated and are characterized by attention to customer service, lower fees and small business, agricultural and consumer lending. ICBA's members hold more than $526 billion in insured deposits, $643 billion in assets and more than $402 billion in loans for consumers, small businesses and farms. For more information visit www.icba.org.

Our testimony addresses the following areas covered by the proposed rule: Mortgage Broker Compensation; HUD's Good Faith Estimate (GFE) settlement cost disclosure; and Guaranteed Mortgage Packages.

Mortgage Broker Compensation

The proposed rule calls for a change in the manner in which lender payments to brokers are recorded and reported to consumers. Specifically, the rule would require that for loans originated by mortgage brokers, any payments from a lender based on a borrower's transaction, would be reported on the Good Faith Estimate (GFE), and the HUD-1/1A Settlement Statement as a lender payment to the borrower, including payments based on an above par interest rate on the loan (including yield spread premiums). Similarly, any borrower payments to reduce the interest rate (discount points) in brokered loans must equal the discount points paid to the lender, and be reported as a borrower payment to the lender. HUD believes that this change will resolve disputes regarding broker compensation, and improve the process of obtaining a home mortgage.

ICBA fully supports disclosure of broker compensation in mortgage loan transactions. However, it is our view that this proposed change would neither resolve the current broker compensation issues, nor accomplish the goal of improving the process. Reporting broker compensation as proposed will not result in a simpler more transparent process, but will instead result in more confusion for the borrower. We believe that retention of the existing disclosure requirements would prove far less confusing.

HUD's Good Faith Estimate Settlement Cost Disclosure

The proposed rule also calls for a change in the existing RESPA disclosure scheme through a new format for the Good Faith Estimate (GFE). The goal is to create a consumer friendly form providing borrowers with more useful and accurate information to assist them in the mortgage finance process. The rule proposes more precise cost estimates than what is currently required. These estimates would be grouped by category with a zero tolerance level for some items, except in the event of unforeseeable and extraordinary circumstances, and a ten percent tolerance level for others. While HUD considers this an enhancement to aid the borrower, we believe it will affect both borrower and lender by ultimately resulting in an increase to the cost of loan packages, and will negatively impact the ability of community banks to compete in this arena.

Certain costs are much easier for loan originators to estimate than others, and certain costs set by third parties are difficult for a lender to guarantee. For example, loan originators generally know, with certainty, the cost of a credit report. However, situations often arise for consumers with unusual credit histories when additional information must be verified causing the costs to unexpectedly increase. This may especially be the case with recent immigrants or minorities who do not have traditional credit histories, the very individuals the Bush administration is trying to reach, and the very individuals who reside in the communities served by our member banks. Similarly, a loan originator may order a property survey or appraisal expecting that, based on experience, it will cost a certain amount that can be guaranteed, but find that once work has begun, the property requires additional surveys or appraisals at an additional cost. Both of these are examples of costs that under the proposed rule would fall in the zero tolerance rate category, and would, therefore, have to be guaranteed by the loan originator who would also be required to absorb any and all unexpected or additional costs. Aside from the two previous examples, there are several other zero or ten percent tolerance rate items that may vary depending on the final loan amount and closing date, both of which can change at the request of the borrower, yet any resulting increase in costs will again be absorbed by the lender. This will naturally result in loan originators increasing the costs of packages to all borrowers to guard against such contingencies

Moreover, all service providers do not charge the same amount for their services. Our community banks generally use the lowest cost provider. However, for reasons beyond the bank's control, that may not always be possible. There will be times when the preferred provider is unavailable or too busy to ensure that the requested work is completed according to the borrower's schedule. The precise cost estimates and guarantees required under the proposed rule will place banks between the proverbial rock and a hard place. They will either have to quote the highest rates and price themselves out of the competitive mortgage finance market or attempt to remain competitive while running the real risk of having to absorb those unexpected and additional costs. We believe that the firmness of the cost estimates proposed by HUD does not adequately reflect the variances that legitimately occur in the industry. Loan originators should be required to document changes to justify increases in the cost of items at settlement, but locking them into fees at the application phase can only result in increased costs.

Finally, the instructions to "Attachment A-1" of the revised forms requires loan originators to itemize services that the borrower can shop for, and estimate the cost of these services ". . .based on local market averages for the areas where the property is located." It is our view that the requirement to collect and maintain data to determine market averages is an unreasonable and burdensome expectation, particularly for small originators located in large metropolitan areas. We believe a better approach would be to require that the originator insert the estimated cost of the service as if they were providing it.

As you can see, the proposed enhancement to the GFE will impact both borrowers and originators in a manner that will be contrary to the rule's objectives.

Guaranteed Mortgage Packages

Finally, the proposed rule seeks to facilitate mortgage shopping and promote competition by removing the regulatory barriers to allow a safe harbor under RESPA for Guaranteed Mortgage Package transactions. A Guaranteed Mortgage Package (GMP) consists of a mortgage loan with a guaranteed interest rate and a package of settlement services required by the lender to close the mortgage. The settlement services would include, but are not limited to, all application, origination and underwriting services, the appraisal, pest inspection, flood review, title services, title insurance and any other lender required services except hazard insurance, per diem interest and escrow deposits.

Unlike the GFE, a GMP would not itemize the specific services to be provided. HUD believes that the GMP will make it easier for borrowers to shop for mortgages through simpler more transparent transactions, and will further reduce settlement costs as a result of market forces, borrower shopping and competition. It is our position that the GMP will take away the borrower's opportunity to shop for those items included in the package. Further, because all services are packaged, there would be no assurance to the borrower as to what will and will not be provided. This will, in effect, eliminate comparison shopping, one of the essential elements of the process that this rule seeks to promote.

In addition to the package of settlement services, a GMP must include a guaranteed interest rate that is tied to an observable index or other appropriate means that would assure borrowers that if the lender increased the rate, it was not driven by the lender's desire to increase its origination profits. This proposed change is simply unreasonable in that it does not reflect the realities of the mortgage industry, and how interest rates are set and how quickly they can change in the course of a day. The rule also assumes that lenders and brokers control the interest rates they offer which, in most situations, is simply not the case. Interest rates offered by community banks are often set by the secondary market organizations or lenders that purchase the loans. HUD's proposal that brokers or lenders guarantee rates without any type of financial commitment from the consumer while the consumer is free to shop for the best package, unreasonably exposes the brokers and lenders to interest rate risk. The cost of this risk will either be borne by the banks or the borrowers. To protect itself against interest rate risk the institution will incur additional expenses that can be recouped only if the consumer returns for the loan, or consumers may bear the cost of higher rates imposed by the institution.

Further, the requirement that loan originators must post and constantly update mortgage rates on their website would be very costly and highly burdensome for community banks. First, not all community banks have websites, and secondly of those that do, few offer the ability to apply for mortgage loans. ICBA recently completed its 2002 Annual Community Bank Technology Survey.[2] Seventy three percent of community banks responding maintain an internet site, and of that group, seventy four percent offer some banking services through the site. However, most services offered by community banks through internet websites relate to account information with only about thirty percent of respondents indicating that they offer their customers the ability to apply for loans through their website. Therefore, it appears that the larger lenders are in a better position than many community banks to comply with the proposed interest rate posting requirement.

Loan originators should not be forced to make unnecessary and expensive expenditures for technology. Requiring lenders to post an interest rate index is impractical, and may not serve as a reliable tool for consumers. Some loan originators offer only a handful of loan products, while others may have dozens of products and rates. Moreover, interest rates can change within a day during volatile periods. The effect of compliance on smaller financial institutions would be enormous, and would force many to exit the market altogether. The significant resources that would be needed to maintain current data, could be better allocated to originating and processing mortgage loans and marketing to those minority families the Bush administration has targeted for homeownership.

Finally, to allow packagers to offer the GMP, the rule provides a safe harbor from RESPA Section 8. Therefore, the very provisions that were developed to protect consumers from special fee arrangements between settlement service providers and loan originators do not apply. Proponents of this safe harbor provision believe that it is necessary in order to offer the GMP and lower mortgage costs. However, nothing in the proposed rule indicates that the cost savings would be passed along to the borrower. ICBA views this as a complete reversal, and an exposure to the risk that we will return to the environment of abusive practices that RESPA Section 8 was originally designed to prohibit.

ICBA has repeatedly raised concerns about the effect the HUD proposal will have on the ability of smaller banks and service providers to compete against the larger market participants. We agree with HUD's premise that consumers benefit when they have choices. However, it is clear that the proposed rule will eliminate consumer choice in that the smaller, and lower volume generating lenders, brokers and settlement service providers will be driven from the market because they simply will not be able to negotiate the necessary discounts from settlement service providers to compete with the larger institutions in offering GMPs. We strongly believe that is it wrong for a government agency to regulate institutions out of an industry simply because of their size. This is clearly a rule that favors the largest institutions in the mortgage industry.

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[2] The survey was sent to over 9,000 community banks with over a ten percent response rate. Those banks responding had an average asset size of $160 million.

Community banks are also concerned that the GFE and GMP requirements will limit their ability to provide early credit counseling, and to offer alternative products that may better suit the borrower's needs. Should HUD feel compelled to move forward with the GMP, it should only do so as a test while making no changes to the current GFE. Currently, several institutions are marketing versions of a guaranteed package. We see this as the best way to proceed – allow the market to continue its evolution without regulatory mandates to packages.

In conclusion, the ICBA has grave concerns that HUD's proposed changes to RESPA will seriously undermine the mortgage finance process, and reverse the trend of overall homeownership growth. While HUD believes this rule will simplify and improve the process of shopping for mortgage loans, ICBA feels strongly that this will not be the case. This proposal will dramatically alter the manner in which mortgages are offered, making the process more confusing, impacting consumer choice in the selection of individual settlement services, and decreasing consumer options for mortgage products. It will also inevitably create an environment where the largest originators and settlement service providers will drive out the smallest.

If this rule is adopted, it will result in a serious disruption of the mortgage finance process, and increase, not decrease as HUD predicts, the cost of homeownership. ICBA opposes the proposed rule because of the damage it will do to consumers, the mortgage finance system, and the small loan originators and settlement service providers that participate in it. Accordingly, we strongly urge the Committee to encourage HUD to reconsider the proposed rule, and to proceed cautiously and slowly to avoid a disruption of the mortgage finance process, and a negative impact on consumer choice and homeownership growth overall.

Thank you for the opportunity to submit testimony today. ICBA stands ready to work with the Committee on this important issue.

NATIONAL ASSOCIATION OF REALTORS®

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February 25, 2003

The Honorable Bob Ney
Chairman
Subcommittee on Housing & Community Opportunity
U.S. House of Representatives
Washington, D.C. 20515

Dear Chairman Ney:

On behalf of the National Association of REALTORS® (NAR), I appreciate the opportunity to submit to the House Financial Services Housing Subcommittee our thoughts on HUD's proposed rule to reform the Real Estate Settlement Procedures Act (RESPA). NAR is America's largest trade association, representing more than 860,000 members involved in all aspects of the residential and commercial real estate industries. When it comes to the home purchase transaction, REALTORS® hold the position closest to the consumer. From the very early stages of the home search to closing day, the REALTOR® is involved and acts as an advisor in the process. It is because of this very important role that we feel we can offer valuable insight into how these proposed changes may impact the consumer as well as the industry.

NAR supports efforts to improve RESPA and the home mortgage transaction experience for consumers. We admire Secretary Martinez's dedication to this initiative and we appreciate and agree with the stated goals of reform as set forth by the Department: 1) to simplify and improve the process of obtaining home mortgages, and 2) to reduce settlement costs for consumers. However, I will state up front, we have serious reservations as to whether the proposal as written meets these goals.

As you know, this proposal has generated significant response from all segments of the industry and consumer groups. In fact, only now that the comments are in can we truly appreciate the complexity of this proposal. While some may endorse the concept of the GMP, support is conditioned on the adoption of recommended changes and these changes are as numerous as the number of groups making them. How HUD responds to these recommendations will determine the level of future support or opposition. Unfortunately, the current process does not permit the industry to reassess the proposal relative to any changes HUD might consider upon review of the 45,000 comment letters. Therefore, we think HIUD should consider amending their proposal based on industry and consumer comments and to put it out again for additional comment.

NAR Position

I will summarize our overall reaction to this proposal, which we submitted in our comments to HUD.

- HUD proposes two new disclosure methods, the Guaranteed Mortgage Package (GMP) and the Enhanced Good Faith Estimate (GFE). We believe the goals of reform can be achieved by improving the current Good Faith Estimate (GFE). While the proposal before us must be more carefully constructed, we support the concept and recommend that further analysis and development of this concept be conducted.

- The Guaranteed Mortgage Package (GMP) represents a radical departure from today's rules. There is not enough evidence of consumer and industry benefit to move forward with this at this time. Additional data collection, research and analysis need to be conducted to provide evidence of significant benefits. There are risks inherent in this proposal and until more is known about the likely impacts, HUD should postpone advancing this kind of significant regulatory change.

- Congress should address many of the changes to RESPA in this proposal. To propose a repeal of Section 8 or to require providers to fix their fees requires oversight by the body that created RESPA.

The Enhanced Good Faith Estimate (GFE)

The goals of reform, certainty and simplicity, can be achieved without sacrificing the important consumer protections of Section 8. The Enhanced GFE consolidates costs into categories and imposes pricing discipline on lenders thus providing borrowers more certainty early in the process enabling them to shop and compare loans. It also clarifies that volume discounts are permissible, thereby encouraging lenders to seek discounts that can be passed on to consumers.

This incremental approach will reduce the potential for any market disruption and will pave the way for future changes as appropriate. Specifics of this approach should be carefully studied to minimize burdens on the industry, such as the tolerances for those services not within the control of the lender. Clarifying that volume discounts are not a violation under RESPA should go a long way toward providing lenders who otherwise would not be inclined to seek these discounts for their customers. Additional thought on the mortgage broker compensation disclosure should also be more fully analyzed so the broker is not unfairly placed at a competitive disadvantage to a retail lender. There could also be small business implications that require additional scrutiny. The GFE form should be further reviewed and amended so borrowers can more easily reconcile it with the HUD-1 at closing. Additional thought must be given to the proposed penalties for non-compliance. To simply permit the borrower to walk away at closing is a disservice to everyone in the transaction including the borrower. Penalties must be stiff enough to discourage non-compliance and rational to ensure innocent parties to the transaction are not penalized. These improvements to the GFE will go a long way toward achieving the stated goals of the Department and are consistent with the original purpose of RESPA.

The Guaranteed Mortgage Package (GMP)

While being characterized as an improvement to the process, the GMP could produce unintended consequences for the consumer, the lending and entire settlement service industry. It could also negatively impact the overall economy. The proposal assumes an increase in competition will result from the packaging scheme and this competition will drive down prices and benefit consumers. However, we believe there is also the possibility that this proposal could increase concentration, reduce transparency, reduce the quality of services, and ultimately lead to higher closing costs. This will undoubtedly alter the lending and settlement services industries. We come to this conclusion after carefully weighing the benefits of the available reform options against the potential for negative market consequences due to the loss of RESPA's Section 8 consumer protections. What amounts to broad relief for one segment of the industry without evidence of consumer benefit or continued consumer protections represents a flawed approach to reform and should be revisited.

At first glance, the prospect of creating a simplified disclosure that includes an interest rate and lump sum closing costs at no cost to the consumer is appealing. However, upon further review, we find there are too many unanswered questions and concerns about this approach. The following is a summary of some of these concerns in the proposal.

The GMP limits packaging to lenders-The very first observation I would make is that the proposal states, "anyone can package." It is misleading for HUD to suggest this while also requiring that the packages be advertised with a guaranteed interest rate. The only players in the marketplace that can offer a guaranteed interest rate are the lenders. This is confirmed in another provision that requires the GMP to be signed by a lender. Therefore, real estate brokers will only be able to offer packages if they form a relationship with a lender. Even then, the terms of the relationship and the package arrangements will be subject to the specific lender requirements. They will not be able to market their services directly to consumers. Packagers will always be under the control of the lender. Therefore, the rest of my comments will reflect the lender as the intended packager.

Simplification- The proposed GMP disclosure includes the interest rate, APR and a lump sum package price for settlement services. However, there are three other required settlement costs that are not included in the package and disclosed separately. They are per diem interest, reserves/escrow, and hazard insurance. In addition, there is an optional owner's title insurance disclosure. While it may be easy enough to add these costs to the lump sum GMP, we must not assume how the final rule will reflect these disclosures. In public comments to HUD, several lender groups have advocated the removal of some of the services within HUD's GMP and to disclose them separately. Some of the services they recommend to exclude from the package are flood insurance, mortgage insurance, government fees and points. If HUD agrees with this assessment, the disclosure becomes very complicated. So the new disclosure would include the cost disclosures for the interest rate, points, the guaranteed package, per diem interest, reserves, hazard insurance, mortgage insurance, and flood insurance. Under this scenario, there may be more services outside than inside the guaranteed package.

Interest Rate Guarantee- The HUD GMP proposal requires an interest rate guarantee, subject to change resulting only from a change in an observable and verifiable index and it must remain open to the potential borrower for thirty days. The reason for linking the two is to prevent a lender from increasing the interest rate to make up for any losses on the guaranteed package. While lenders may find the 30-day interest rate guarantee unworkable, to deviate from this requirement will undermine the rationale for the GMP in the first place. To guarantee one piece of the offer and not the other can lead to bait and switch tactics and other abusive practices. Therefore, additional analysis is required to assess the impact of guaranteeing the interest rate.

Certainty of costs-HUD has indicated one of its goals in this proposal is to protect consumers by providing some cost certainties in the mortgage transaction, hence the "guarantee" in the GMP. The rule, however, appears to have a loopholes that negates the contractual "guarantee," specifically, the condition of "pending final underwriting and appraisal." Under this proposal, there is nothing to prevent a lender from trying to lure consumers with a below-market GMP, and then increase the interest rate or costs following final underwriting, which can take place right up to the closing. Therefore, it is questionable as to whether the consumer is truly getting a guarantee. It sounds more like a conditional guarantee.

Transparency In the Process- In the HUD proposal there is much emphasis placed on creating a transparent process. However, the GMP will result in quite the opposite. Borrowers will shop for a loan based on an interest rate and a "black box" of settlement costs. To move from a process today where borrowers are fully informed of the various services required to close the transaction to one in which the borrower is assumed to only be interested in the lump price of the package is taking a step backwards in the area of consumer education. Despite claims to the contrary, consumers want to know what they are getting for their money. If services are not disclosed to the borrower, true comparisons cannot be made. Even in the 1998 HUD/Fed Report, they recommended that *"consumers want to know what services they are purchasing... "*, and so they suggested the services in the package be itemized.

If nothing else, HUD needs to recognize this flaw in the proposal. Both services and quality of services matter to consumers. While lenders contend that these services are for their use, the borrower pays for them and is directly impacted by the quality of the service providers. For example, a lender may have a contract with a certain pest control company and includes this service in its package. The pest control company may not be very reputable yet meets the minimal needs of the lender. Substandard work could mean problems in the future that may result in thousands of dollars for the homeowner.

In the purchase money market, most borrowers rely on trusted advisors, such as real estate agents in the selection of settlement services. Under today's rules that prohibit settlement providers from paying or accepting fees for the referral of business, the only driving force behind a referral of business from a real estate agent to another provider is continued customer satisfaction from trusted providers in the marketplace. It is widely acknowledged that if a borrower is not satisfied or has a negative experience with a certain provider in the transaction, it is the real estate agent who must make things right. Under HUD's GMP proposal, the ability to guide the borrower through the transaction is restricted by these pre-arranged packages where services are not disclosed and service quality may be at risk. As pressure mounts on settlement providers such as appraisers, title companies, pest inspectors to drastically cut their prices to ensure inclusion in a lender package, quality of service could deteriorate. This scenario further underscores the need for full disclosure of services in a package.

Increased Competition or Increased Concentration

There is the likelihood that HUD's packaging proposal can lead to increased concentration within the industry and reduce competition. Lenders will be provided a financial incentive (section 8 exemption) to package with no obligation to pass along discounts to borrowers and as a result will control the entire mortgage transaction. This will most likely lead to increased market share of the large lenders who already control the lion's share of the mortgage origination and servicing market. Small service providers including real estate brokerages with ancillary services will be at risk. Today the real estate transaction is still very much locally based. Small and mid-size service providers offer competitive choices to borrowers.

Any regulation that moves an industry toward a more concentrated market structure should be viewed with considerable caution. An increased concentration of powers into the hands of a smaller number of large lenders and service providers could lead to higher closing costs—the exact opposite of HUD's stated goals for reform.

Alternative to the GMP

We strongly believe there are serious flaws in the GMP proposal and believe they should instead pursue changes to the GFE that will provide some certainty about costs and simplify the process. However, if HUD is committed to moving forward with a Guaranteed Packaging rule as outlined in their proposal, we recommend a restructuring of the GMP. If the intent is to promote competition among non-lender packagers, a mechanism must be designed that will truly allow anyone to package independent of the loan. If designed correctly, it may offer opportunities for non-lender packagers, such as real estate brokers, title companies and others to provide alternative choices for the consumer, which do not exist under this proposal.

To date it appears the only alternative that would meet this objective is to split HUD's GMP into two independent guaranteed packages:

1) Lender Service Package: This package would include the lender services and perhaps the appraisal and credit report (800 series services on the HUD-1), and
2) Closing package: This package would include all of the other services such as title, inspections, surveys, government fees, etc. (1100, 1200, 1300 series services on the HUD-1).

Under the two-package system, a lender could offer a lender package along with a guaranteed interest rate. Anyone, including non-lenders, such as real estate professionals could offer the closing package. The conditions for receiving the Section 8 safe harbor would have to be carefully defined. Some minimal requirements would include:

- A lender could not require a borrower who is obtaining the lender's loan and lender package to also purchase the lender closing package. In other words, the lender cannot tie their loan to a particular closing package.
- The services within the packages, both the lender and closing cost packages, would be itemized. Upon request of the borrower, the service providers should also be disclosed.
- Lenders should provide copies of all reports to borrowers, i.e. credit report, appraisal, etc. Lenders should also disclose to borrowers the type of appraisal used by the lender, i.e. Automated Valuation Model (AVM), a drive-by, or a full appraisal.
- HUD should move toward adopting and requiring uniform service fee descriptions so borrowers can make apples to apples comparisons.

Under this proposal, large lenders will still have a competitive advantage with the Section 8 exemption. However, it is anticipated the lender tying prohibition of the closing package will provide a non-lender some opportunity to compete in this market by offering these services directly to the consumer. The details of such a proposal requires further development and analysis to ensure it creates adequate opportunity for other market players to compete. Further, if HUD pursues this disclosure track, then it would be appropriate to delay implementation of the Enhanced Good Faith Estimate.

Conclusion

The above issues argue the need for additional study on this proposal, the need for alternative approaches to the GMP, and its impact on the consumer as well as the industry. Not enough is known about the likely impact of the GMP to support advancing this concept at this time. An incremental approach, such as the improved GFE is a more attractive option for satisfying HUD's stated goals for reform. By simplifying the GFE and clarifying that volume discounts are not violations of RESPA, HUD has created the necessary environment for packaging to occur.

Regardless of which approach to reform HUD endorses, Congress should be consulted before any final action is taken. We are very supportive of these Congressional hearings and would like to serve as a resource as the Committee continues to review this proposal. There is too much at risk to move forward in a less than thoughtful and deliberative manner. While we support the concept of the Enhanced GFE, we question whether HUD has the authority to require lenders to guarantee their fees. Similarly, repealing Section 8, a core provision of RESPA, should receive considerable debate on Capitol Hill by the body that created it in the first place. What

Congress deemed a prohibited practice, HUD recommends looking the other way as long as the prices are guaranteed.

Let me conclude by calling to your attention HUD's statements in the proposed rule under the Supplementary Information Section

"The American mortgage finance system is justifiably the envy of the world. It has offered unparalleled financing opportunities under virtually all economic conditions to a very wide range of borrowers that, in no small part, have led to the highest homeownership rate in the Nation's history"

This statement should serve as a reminder that before HUD moves forward with an untested model, it must be sure it does not jeopardize a system that despite its flaws is still working well for most Americans.

In light of this, we encourage further development of the Enhanced GFE concept as a means to make incremental changes to a system that we know and understand. If this were not a viable option, then we would strongly recommend further analysis and development of a two-package approach to the GMP. Unless there is a real opportunity for providers other than lenders to offer packaged settlement services to consumers, the negative consequences of HUD's proposed GMP will far outweigh any potential benefits to consumers.

I thank you for the opportunity to express the views of the National Association of REALTORS® and stand eager to work with Congress to further address these issues.

Sincerely,

Catherine B. Whatley

Cathy Whatley

The Wall Street Journal

Monday, February 24, 2003

Take-Home Pay: The Refinancing Boom Spells Big Money for Mortgage Brokers

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Huge Fees Draw the Scrutiny Of Regulators and Spawn Lucrative Small Companies

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From Machinist to Millionaire

By **John Hechinger**

WALPOLE, Mass. -- Tom Digan doesn't have to make a hard sell these days to cash in on the mortgage boom. He just needs to pick up the phone.

In his small office, overlooking an auto-repair shop, the 44-year-old mortgage broker returns a call from a customer who wants a $240,000 loan -- one of 50 to 150 daily calls that jam his voice mail. Mr. Digan checks a sheet on his desk, calls up an online credit report and offers a great rate: 5.5% on a 15-year mortgage. "I'll write it up right now," he says, scribbling financial information on an application.

Once the loan closes, Mr. Digan and his employer will split a fee that might make a corporate lawyer do a double take: $2,800. "I know what you're thinking," Mr. Digan says. "He made $1,400 in 15 minutes."

Such transactions have turned the nation's 40,000 mortgage brokerages into some of the most profitable small businesses in America. These low-profile companies don't lend money -- they find loans for consumers in exchange for commissions. These days, brokers are racking up fees that rival Wall Street's 1990s windfalls.

In this blue-collar Boston suburb, Mr. Digan's employer, Mortgage Master Inc., brokered 11,000 loans last year, valued at $3 billion, more than four times the amount just two years before. From his cut of commissions, the firm's owner, Leif Thomsen, who left school at 14, earned $10 million last year.

Five brokers at Mortgage Master earned more than $1 million last year, including Mr. Digan, the top salesman, who took home $1.7 million -- 10 times his best year at his former job, selling electrical equipment. Many others got paychecks in mid- to high- six figures, including a former truck driver who made almost half a million dollars.

Mortgage brokers have been beneficiaries of an unprecedented boom in home- loan refinancings, spurred by interest rates that have dipped to their lowest levels in decades. Of the $2.5 trillion in mortgages taken out last year, roughly 60% was handled by the nation's 120,000 brokers, up from just 20% in 1987, according to David Olson, managing director of Wholesale Access Mortgage Research & Consulting Inc., which conducts extensive industry surveys. Other industry analysts peg brokers' market share at 40%.

Last year, the average mortgage broker made $120,000, while owners of brokerage firms took home $400,000, Mr. Olson calculates. Both figures are double the levels of only two years ago. At least 5%, or some 6,000 brokers, earned $1 million or more.

Unlike many high-paying professions, mortgage brokers typically aren't required to have much more training than what they get on the job. Although mortgage firms generally need a state license, only 13 states require them for individual brokers.

The light regulation and huge fees have federal housing regulators concerned that consumers may be paying too much. So they are poised to pass new disclosure rules that could make it easier for consumers to compare brokers' commissions and consequently drive them down. In addition, more than a dozen states and cities have passed predatory-lending laws designed partly to restrict the sometimes-astronomical broker fees charged to consumers with poor credit histories.

Even the most bullish brokers acknowledge that their incomes are likely to fall from last year's record levels, because many believe interest rates are near their lows and sooner or later most homeowners won't be able to save money by refinancing. But if loan originations drop by 19% this year -- as the Mortgage Bankers Association of America predicts -- 2003 will still be the third-best year on record.

Only recently have mortgage brokers become a force that would merit scrutiny. Until the 1970s and 1980s, savings-and-loans dominated the mortgage business. A customer typically would see a loan officer at a local branch, and the lender would often hold mortgages for 30 years.

But the mortgage business has been transformed into a largely high-volume, national market. Instead of holding on to mortgages, lenders tend to sell them in big bundles, often through government-sponsored mortgage firms Fannie Mae and Freddie Mac. In turn, Fannie and Freddie in the 1990s developed automated underwriting systems that allow quick approval of mortgages. Often, customers are asked for little more than a credit report, a pay stub, a bank statement and a few tax forms.

These changes turned selling mortgages into a commodity business, letting brokers compete on an equal footing with banks. Many of the biggest lenders, such as Washington Mutual Inc., Wells Fargo & Co. and Countrywide Financial Corp., make extensive use of brokers. The brokers allow the big lenders to extend their own sales forces and offer a low-cost way to tap into broader markets.

For the high-volume broker, the economics are compelling. On average, a broker pockets the equivalent of 1% to 1.5% of a mortgage, industry analysts say. Sometimes these fees come in upfront payments from borrowers. In other cases, brokers get their commissions from lenders, which pay a premium for a mortgage with an above-market interest rate.

That's what happened in the case of the $240,000 mortgage sold by Mr. Digan of

Mortgage Master. The customer wanted a no-cost loan, even though that raised her rate by one-quarter percentage point. Because the loan was at an above- market rate, the lender will pay Mr. Digan's firm a commission equal to 2% of the loan amount, or $4,800. Out of that, the brokerage firm will pay $2,000 in closing costs, such as attorney and appraisal fees. Mortgage Master and Mr. Digan will split the rest, $2,800.

The most successful brokers tend to toil in hot markets with high real-estate values, including New York, California and Massachusetts. One of New York's premier brokers is Melissa Cohn, who runs an 80-broker shop from offices on Madison Avenue. Her firm, Manhattan Mortgage Co., finances multimillion dollar Park Avenue co-ops and posh summer homes. A 42-year-old former Citibank loan manager, Ms. Cohn says she had a "seven-figure income" last year but won't be more specific. She networks at charity galas, jumps horses competitively and owns a 24-stall horse barn in Bridgehampton on Long Island. "Last year was absolutely insane," she says.

Far from big cities, brokers are also thriving. At Benchmark Mortgage Inc. in Richmond, Va., 33-year-old Robert Roland, a former machinist, says he made more than $1 million last year. "I never thought I'd be making money like a professional athlete," he says.

Critics say the fees have gotten out of hand. Howell Jackson, a Harvard Law School professor who has studied the industry, says mortgage brokers shouldn't be paid more than doctors and lawyers. His research suggests that $1,600 would be a fair fee, no matter the size of the loan. He figures that would cover the broker's cost and still provide a reasonable profit. But brokers will often charge twice that sum. "These are supra-normal profits," he says.

Concerned about the possibility of abuse, the U.S. Department of Housing and Urban Development is considering new rules that could require mortgage brokers to disclose early in the process how much they are paid for a loan -- an estimate that would be binding in most cases -- so shoppers can compare prices more easily. Under current rules they must give a "good faith" estimate of commissions, but a customer can be surprised with a higher fee when handed the final paperwork.

The magnitude of the fees don't always get close attention from borrowers. They tend to be concerned with a single mortgage figure: the amount they'll need to write on a check each month. The broker fees, often built into that monthly total, can also get lost in the avalanche of papers that need to be signed at a typical closing.

Jack Guttentag, professor of finance emeritus at the University of Pennsylvania's Wharton School, says improved disclosure could cut brokers' fees in half because it's fairly difficult to comparison-shop for mortgages now. HUD's disclosure proposal could hit brokers "in the solar plexus," he says.

Armand Cosenza Jr., president of the National Association of Mortgage Brokers, says so many brokers and lenders are vying for customers in a competitive market that anyone who shops around will get a fair deal. He says the American homeownership rate wouldn't have reached a record 68% without the unfettered efforts of brokers, many of them self-made small-business owners.

That's an apt description for Mr. Thomsen, the 42-year-old founder of Mortgage Master. Born in Denmark, the son of a math teacher, Mr. Thomsen was a restaurateur and worked briefly as a mortgage broker in suburban Boston before starting his firm in 1988 in a spare bedroom. In his first year, he sold $50 million in loans, reaping $500,000 in commissions.

"I remember calling people back in Denmark and saying, 'You're never going to believe this business I've gotten into,' " he says.

These days, Mr. Thomsen's firm is literally a financial factory. Mortgage Master last fall moved into a brick building, a former paper mill in Walpole, Mass., a 35-minute drive southwest of Boston. Top-producing brokers have small offices with windows, surrounding a warren of cubicles packed with newcomers and a support staff of 100.

The operation last year handled 100 or more mortgages on a busy day. A typical loan takes about six hours to process and underwrite, in addition to a couple of hours of a broker's time to sell, take an application and follow up with customers. Mortgage Master says it generated $30 million in fees last year, after paying closing costs for some of the mortgages. Support staff, rent and other overhead ran $5 million, or about $500 a loan. The rest was distributed as commissions among Mr. Thomsen and his brokers.

Four years ago, Mark Shippie was driving a Pepsi truck when he was refinancing his own loan and noticed that his Mortgage Master broker was driving a luxury car. He begged Mr. Thomsen for a chance to strike it big. "Do you really want to quit a steady job?" he recalls Mr. Thomsen telling him.

Mr. Shippie did, and he jumped into his Ford pickup and hit up everyone he knew for mortgages, driving 45,000 miles in his first year. He called people at Pepsi and Coke, left his cards at Dunkin' Donuts and dropped by fire and police stations across suburban Boston. Since then, he has managed to build a database of 1,200 customers, the key to success as a mortgage broker.

Last year, Mr. Shippie sold $97 million in loans and made $480,000, 10 times his pay at the soda company. He now lives in a $700,000 home and has a $200,000 condo in New Hampshire. "I'm set for the rest of my life," says Mr. Shippie, 45, wearing a hooded sweat shirt in his windowless office.

Once a broker makes a sale -- "locks" a loan, in broker's parlance -- he or she drops the application in the inbox of the "lock desk," in many ways the nerve center of Mortgage Master. Mr. Thomsen sits at the lock desk, wearing an open collar shirt, blue jeans and leather slippers. He repeatedly checks blinking bond prices on a computer screen. He's trying to guess the direction of interest rates to see whether his brokers should rush loan documents to lenders now, or wait until later in the afternoon.

Lenders generally send in rate sheets daily to Mortgage Master and other brokers, but can modify them at any time if interest rates change, often by increments as tiny as one-eighth of a percentage point. On this day, rates have been ticking up on news about Iraq and economic data. Mr. Thomsen gets an alert that one lender, the finance unit of General Motors Corp., is raising its rates. "GMAC is repricing for the worse," he shouts.

Year after year, Mortgage Master employees pack the top of lists ranking highest-producing brokers from Mortgage Originator and National Mortgage News, two trade publications. In 2002, Mortgage Master says, every broker who worked a full year at the firm pulled in a six-figure income.

Mr. Digan, Mortgage Master's top producer, has built up an impressive list of 6,000 clients. To get started, he focused on real-estate agents and potential buyers. He'd even pay hundreds of dollars to provide food for Sunday open houses, and then stand at the events handing out his business card and rate sheets.

These days, Mr. Digan rarely leaves the office. The soft-spoken 6-foot-3 salesman can even knock off early some days to play wing in an amateur ice- hockey league, returning calls on his cellphone. Last year, he wrote more than 1,000 loans, with a total value of $310 million.

Many are repeat customers, such as Bradford Smith, a senior partner at Boston law firm Goodwin Procter LLP. In nine years, Mr. Smith has bought four homes and refinanced 12 times, all through Mr. Digan. Mr. Smith says one refinancing took only an hour, including 40 minutes with his attorney at closing. Mr. Smith, a litigator who bills $425 an hour, realizes Mr. Digan's fees are quite similar. "I can't begrudge him," Mr. Smith says. "He works hard. He's one of the big hitters."

---- INDEX REFERENCES ----

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