Billing Code 4210-67-P
DEPARTMENT OF HOUSING AND URBAN DEVELOPMENT

24 CFR Parts 203 and 3500

[Docket No. FR-5180-F-03]
RIN 2502-AI61

Real Estate Settlement Procedures Act (RESPA): Rule to Simplify and Improve the Process of Obtaining Mortgages and Reduce Consumer Settlement Costs

AGENCY: Office of the Assistant Secretary for Housing—Federal Housing Commissioner, HUD.

ACTION: Final rule.

SUMMARY: This final rule amends HUD's regulations to further RESPA's purposes by requiring more timely and effective disclosures related to mortgage settlement costs for federally related mortgage loans to consumers. The changes made by this final rule are designed to protect consumers from unnecessarily high settlement costs by taking steps to: improve and standardize the Good Faith Estimate (GFE) form to make it easier to use for shopping among settlement service providers; ensure that page 1 of the GFE provides a clear summary of the loan terms and total settlement charges so that borrowers will be able to use the GFE to identify a particular loan product and comparison shop among loan originators; provide more accurate estimates of costs of settlement services shown on the GFE; improve disclosure of yield spread premiums (YSPs) to help borrowers understand how YSPs can affect borrowers' settlement charges; facilitate comparison of the GFE and the HUD-1/HUD-1A Settlement Statements; ensure that at settlement borrowers are aware of final costs as they relate to their particular mortgage loan and settlement transaction; clarify HUD-1 instructions; expressly state that RESPA permits

the listing of an average charge on the HUD-1; and strengthen the prohibition against requiring the use of affiliated businesses.

This final rule follows a March 14, 2008, proposed rule and makes changes in response to public comment and further consideration of certain issues by HUD. In addition, this rule provides for an appropriate transition period. Compliance with the new requirements pertaining to the GFE and settlement statements is not required until January 1, 2010. However, certain provisions are to be implemented upon the effective date of the final rule.

DATES: Effective Date: **January 16, 2009.**

FOR FURTHER INFORMATION CONTACT: Ivy Jackson, Director, or Barton Shapiro, Deputy Director, Office of RESPA and Interstate Land Sales, Office of Housing, Department of Housing and Urban Development, 451 7th Street, SW, Room 9158, Washington, DC 20410-8000; telephone number 202-708-0502. For legal questions, contact Paul S. Ceja, Assistant General Counsel; Joan Kayagil, Deputy Assistant General Counsel; or Rhonda L. Daniels, Attorney-Advisor, for GSE/RESPA, Department of Housing and Urban Development, 451 7th Street, SW, Room 9262, Washington, DC 20410-0500; telephone number 202-708-3137. These telephone numbers are not toll-free. Persons with hearing or speech impairments may access these numbers through TTY by calling the toll-free Federal Information Relay Service at 800-877-8339.

SUPPLEMENTARY INFORMATION:

Background

On March 14, 2008 (73 FR 14030), HUD published a proposed rule (March 2008 proposed rule) that submitted for public comment changes to HUD's regulations

designed to improve certain disclosures required to be provided under RESPA (12 U.S.C. 2601-2617). The RESPA disclosure requirements apply in almost all transactions involving mortgages that secure loans on one- to four-family residential properties. HUD's regulations implementing the RESPA requirements are codified in 24 CFR part 3500. The revisions to the regulations adopted by HUD in this final rule are intended to make the process of obtaining mortgage financing clearer and, ultimately, less costly for consumers.

The preamble of the March 2008 proposed rule presents an overview of the statutory requirements under RESPA, as well as a detailed account of HUD's efforts to initiate regulatory changes commencing in 2002. HUD refers the reader to the March 2008 proposed rule for a detailed description of the background of this rulemaking. The principles that guided HUD in the development of this rule are also included in the March 2008 proposed rule.

The preamble to this final rule highlights some of the more significant changes made at this final rule stage in response to public comment and upon further consideration of certain issues by HUD, summarizes the public comments received on the March 2008 proposed rule, and provides HUD's response to those comments. The following table of contents is provided to assist the reader in identifying where certain topics are discussed in this preamble. This final rule is also accompanied by a final regulatory impact analysis and regulatory flexibility analysis, which are addressed in Sections VIII and IX of this preamble.

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I. Significant Changes from March 2008 Proposed Rule

RESPA is a consumer protection statute, and, as further described in this preamble, consumer groups were, in general, very supportive of the basic goals and key components of the March 2008 proposed rule. For example, the National Consumer Law Center, in a joint comment with Consumer Action, the Consumer Federation of America, and the National Association of Consumer Advocates, stated, "HUD has done an excellent job in moving the ball toward greater protection for consumers in the settlement process." In addition, the Center for Responsible Lending, in its comment concluded: "[W]e applaud HUD for addressing the challenge of reforming RESPA. We believe HUD's proposed GFE provides important improvements over existing requirements."

HUD received adverse comments about many aspects of the proposed rule, primarily from mortgage industry representatives, including requests that HUD withdraw its proposal entirely or that HUD postpone its current efforts in order to work with the Federal Reserve Board to arrive at a joint regulatory approach. HUD takes these comments very seriously and appreciates the concerns raised by these commenters.

HUD's view continues to be, however, that improvements in disclosures to consumers about critical information relating to the costs of obtaining a home mortgage, often the most significant financial transaction a consumer will enter into, are needed, and that such disclosures are a central purpose of RESPA. Most commenters – including consumers, industry representatives, and federal and state regulatory agencies – supported the concept of better disclosures in general, and commended both HUD's efforts and particular provisions in the proposed rule.

Moreover, given the current mortgage crisis, the foreclosure situation many homeowners are now facing because they entered into mortgage transactions that they did not fully understand, and the prospect that future homeowners may find themselves in this same situation, HUD believes that it is very important that the improvements in mortgage disclosures made by this final rule move forward immediately. Nevertheless, as noted in the preamble to the March 2008 proposed rule, HUD will continue to work with the Federal Reserve Board to achieve coordination and consistency between the Board's current regulatory efforts and HUD's requirements.

HUD has made many changes to the March 2008 proposed rule in response to public comment and further consideration of certain issues by HUD. Some of the provisions in the March 2008 proposed rule have been revised in this final rule and others have been withdrawn for further consideration. HUD believes that the result is a final rule that will give borrowers additional and more reliable information about their mortgage loans earlier in the application process, and will better assure that the mortgage loans to which they commit at settlement will be the loans of their choice. At the same time, in recognition of the concerns raised by industry commenters about the need for

sufficient time for the industry to make systems and operational changes necessary to meet the requirements of the new rule, the final rule provides that the new GFE and HUD-1 will not be required until January 1, 2010. However, certain other provisions of the rule will take effect 60 days from the publication date of the final rule. The following are some of the most significant changes made at this final rule stage, and are discussed in more detail in the discussion of public comment.

- A GFE form that is shorter than had been proposed.
- Allowing originators the option not to fill out the tradeoff table on the GFE form.
- A revised definition of "application" to eliminate the separate GFE application process.
- Adoption of requirements for the GFE that are similar to recently revised Federal Reserve Board Truth-in-Lending regulations which limit fees charged in connection with early disclosures and defining timely provision of the disclosures.
- Clarification of terminology that describes the process applicable to, and the terms of, an applicant's particular loan.
- Inclusion of a provision to allow lenders a short period of time in which to correct certain violations of the new disclosure requirements.
- A revised HUD-1/1A settlement statement form that includes a summary page of information that provides a comparison of the GFE and HUD-1/1A list of charges and a listing of final loan terms as a substitute for the proposed closing script addition.
- Elimination of the requirement for a closing script to be completed and read by the closing agent.

- A simplified process for utilizing an average charge mechanism.
- No regulatory change in this rulemaking regarding negotiated discounts, including volume based discounts.

II. Overview of Commenters

The public comment period on the March 2008 proposed rule was originally scheduled to close on May 13, 2008. In response to numerous requests, including congressional requests, to extend the comment period, and HUD's desire to develop a better rule, HUD announced an extension of the comment period. This announcement was made on both HUD's website and by publication of a notice in the Federal Register on May 12, 2008 (73 FR 26953). At the close of the extended public comment period on June 12, 2008, HUD had received approximately 12,000 comments. Approximately two-thirds of the comments received were duplicative or repeat comments; i.e., individuals or organizations who submitted identical or virtually identical comments. For example, members of certain trade organizations, or employees of certain companies, frequently submitted identical comments.

HUD received comments from homeowners, prospective homeowners, organizations representative of consumers, and numerous industry organizations involved in the settlement process, including lending institutions, mortgage brokers, real estate agents, lawyers, title agents, escrow agents, closing agents and notaries, community development corporations, and major organizations representative of key industry areas such as bankers, mortgage bankers, mortgage brokers, realtors, and title and escrow agents, as well as from state and federal regulators.

HUD appreciates all those who took the time to review the March 2008 proposed rule and submit comments.

In addition to submission of comments, HUD representatives accepted invitations to participate in public forums and panel discussions about RESPA and HUD's March 2008 proposed rule. HUD also met, at HUD Headquarters or at the offices of the Office of Management and Budget (OMB), with interested parties, requesting meetings as provided by Executive Order 12866 (Regulatory Planning and Review), who highlighted for HUD and OMB areas of concern and support for various aspects of the rule.

All of this input contributed to HUD's decisions that resulted in this final rule.

HUD also received approximately 100 public comments that were submitted after the deadline. To the extent feasible, HUD reviewed late comments to determine if issues were raised that were not addressed in comments submitted by the deadline.

III. GFE and GFE Requirements – Discussion of Public Comments

A. Overall Comments on the Proposed Required GFE Form

Proposed Rule. HUD proposed a four-page GFE form. The first page of the GFE included a summary chart with key terms and information about the loan for which the GFE was provided, including initial loan balance; loan term; initial interest rate; initial amount owed for principal, interest, and any mortgage insurance; rate lock period; whether the interest rate can rise; whether the loan balance can rise; whether the monthly amount owed for principal, interest, and any mortgage insurance can rise; whether the loan has a prepayment penalty; whether the loan has a balloon payment; and whether the loan includes a monthly escrow payment for property taxes and possibly other obligations. The first page of the form also included information regarding the length of

time the interest rate for the GFE was valid; the length of time the other settlement charges were valid; information about when settlement must occur if the borrower proceeds with the loan; and information concerning how many days the interest rate must be locked before settlement. At the bottom of the first page, the GFE included a summary of the settlement charges. The adjusted origination charges listed on the second page, along with the charges for all other settlement charges listed on the second page, would have been totaled and listed on this page.

The second page of the GFE included a listing of estimated settlement charges. The loan originator's service charge would have been required to be listed at the top of page two, and the credit or charge (points) for the specific interest rate chosen would have been required to be subtracted or added to the service charge to arrive at the adjusted origination charge, which would have been shown on the top of page two. Page two of the GFE also would have required an estimate for all other settlement services. The GFE included categories for other settlement services including: required services that the loan originator selected; title services and lender's title insurance; required services that the borrower would have been able to shop for; government recording and transfer charges; reserves or escrow; daily interest charges; homeowner's insurance; and optional owner's title insurance. The GFE would have required these charges to be subtotaled at the bottom of page two. The sum of the adjusted origination charges and the charges for all other settlement services would have been required to be listed on the bottom of page 2.

The third page of the GFE would have required information concerning shopping for a loan offer. In addition, page three would have included information about which

settlement charges could change at settlement, and by how much such charges could change. Page 3 also would have required the loan originator to include information about loans for which a borrower would have qualified that would increase or decrease settlement charges, with a corresponding change in the interest rate of the loan. (See Section III.B.6 of this preamble below.)

The fourth page of the GFE included a discussion of financial responsibilities of a homeowner. The loan originator would have been required to state the annual property taxes and annual homeowner's flood, and other required property protection insurance, but would not have been required to state estimates for other charges such as annual homeowner's association or condominium fees. The GFE included a section that advised borrowers that the type of loan chosen could affect current and future monthly payments. The proposed GFE also indicated that the borrower could ask the loan originator for more information about loan types and could look at several government publications, including HUD's Special Information Booklet on settlement charges, Truth in Lending Act (TILA) disclosures, and consumer information publications of the Federal Reserve Board. The March 2008 proposed rule invited comments on possible additional ways to increase consumer understanding of adjustable rate mortgages.

Page 4 also would have included information about possible lender compensation after settlement. In addition, page 4 would have included a shopping chart to assist the borrower in comparing GFEs from different loan originators and information about how to apply for the loan for which the GFE had been provided.

Comments

Consumer Representatives

Consumer representatives generally supported the proposed standardized GFE, while offering specific recommendations for improvement. The National Community Reinvestment Coalition recommended inclusion of the annual percentage rate (APR) on the GFE. The Center for Responsible Lending (CRL) stated that it believed that the proposed GFE has the potential to significantly improve current disclosure requirements because it offers a standardized shopping tool with better linkages to the HUD-1, requires that terms be binding, and takes important steps toward trying to alert consumers to the risky features of their loans. However, according to CRL, most consumers will not have the capacity to absorb everything in a four-page GFE and therefore it proposed an alternative two-page GFE.

CRL noted that a new GFE should ensure that consumers have the best chance possible to understand the riskiest features of their loans. CRL commended HUD for adding several features that highlight risk to the first page of the GFE: the prepayment penalty, the balloon payment, the maximum possible loan balance, the maximum monthly payment, and whether certain fees are escrowed. CRL stated that knowing the maximum monthly payment of principal, interest, and mortgage insurance is critical to the consumer's ability to determine whether or not the loan is sustainable. It recommended that other features be added to page 1, including increased emphasis on total monthly payment. It also recommended that the monthly payment amount include an estimate of property taxes, property insurance, and the other charges listed on page 4 of the proposed GFE as one total line item, on page 1.

CRL also recommended that page 1 of the GFE include the annual percentage rate (APR) instead of the note rate because the APR is the standardized measurement of loan

cost in the industry, and because the APR captures the total cost of the loan. CRL further recommended that given that credit cost comprises the largest component of total loan cost, the form's emphasis on settlement costs should be reduced.

In addition, CRL recommended that the first page of the GFE also include information on the first possible date on which the interest rate can rise; an explanation of what prepayment penalties are and how they are triggered; simplified broker compensation; and notification that mortgage terms are negotiable. While CRL supported aggregating fees on page 2 of the GFE to promote mortgage loan shopping, it recommended that the tradeoff table on page 3 be revamped in order to force the rate/point tradeoff that it is intended to disclose.

The GFE proposed by CRL includes the APR, for reasons stated above. In addition, the GFE proposed by CRL includes the first date the interest rate can rise. CRL also included on page 1, "estimated required additional housing expenses" as well as "total estimated maximum monthly housing costs." CRL stated that while it understands that consumers should not compare loans based on total estimated maximum monthly housing costs, CRL believes that it is critical that consumers, particularly those in the subprime market, begin evaluating their ability to afford the loan at the outset of the loan process. CRL's proposed GFE also includes a broader prepayment penalty disclosure than the prepayment penalty disclosure on the proposed GFE. In addition, CRL's proposed GFE includes a broker compensation disclosure, a notice that the consumer can negotiate settlement charges and a summary of charges to facilitate reconciliation to the HUD-1.

Comments by the National Consumer Law Center (NCLC) (filed on behalf of NCLC and Consumer Action, the Consumer Federation of America, and the National Association of Consumer Advocates) stated that the proposed standardization of the GFE, the increased linkage between the GFE and the settlement statement, and the proposed requirement that some terms on the GFE be binding, are important changes that should increase consumer understanding and competition in the mortgage marketplace. NCLC recommended that HUD go further by requiring the prominent disclosure of the APR on the GFE instead of the interest rate. According to NCLC, failure to include the APR on the GFE obscures the cost of credit and hinders consumer shopping.

NCLC expressed concern that the proposed GFE gives far greater prominence to settlement costs than to interest. NCLC stated that if the GFE is successful in getting consumers to shop on settlement costs, there is a risk that consumers will neglect the primary cost component of loans, interest. According to NCLC, while settlement costs matter, they matter most not as a stand-alone cost, but in relation to the interest rate. NCLC recommended that the GFE be revised by reducing the focus on settlement costs through reduction of the font size and elimination of the bold type for settlement costs. NCLC also recommended that HUD work with the Federal Reserve Board to produce disclosures that are not misleading or that obscure the actual cost of credit. In addition, NCLC recommended that the first page of the GFE provide only a total for all settlement costs, without breaking out the origination costs.

NCLC supported the loan summary on page 1 and recommended that the summary sheet refer to the APR instead of to the interest rate. NCLC also recommended

that the first page provide only a total of the estimated settlement charges, not separate lines for the origination and total settlement costs.

Industry Representatives

Generally, lenders and their associations opposed the proposed GFE on the grounds that the form is too lengthy and, in their opinion, would only confuse borrowers. The American Bankers Association commented that the proposed GFE is overly prescriptive. The Mortgage Bankers Association (MBA) stated that the length of the form will cause borrowers to ignore its important information. MBA submitted a two-page GFE as an alternative to the proposed GFE that combines the RESPA and TILA disclosures. While lenders and their associations expressed general support for the goals of the proposed rule, many lenders recommended that HUD work together with the Federal Reserve Board to produce a combined RESPA and TILA disclosure and to implement this combined product simultaneously, to replace the current RESPA and TILA disclosures provided at the time of application.

MBA stated that it generally supports grouping of the amount or ranges of specific services on the GFE in a manner that is comprehensible and comparable, but recommended that the form be modified so that it is mainly a list of charges with minimal supplementary material, as on the GFE form submitted by MBA. MBA recommended that the material on page 3 and page 4 of the proposed GFE be moved to explanatory materials such as the Special Information Booklet. While MBA stated that a summary of loan terms could be useful, it recommended that the summary be removed from the GFE and issued by the Federal Reserve Board in consultation with HUD. MBA further

recommended the deletion of the term "adjusted origination charge" from the bottom of page 1.

A major lender expressed the concern that the proposed form is so laden with information that lenders cannot convey key cost information in a clear and conspicuous manner. This commenter stated that the proposed form would pose a significant compliance burden for lenders and would not provide borrowers with any greater understanding of their loan. Specifically, the lender objected to the disclosures required on page 3 of the proposed form.

The National Association of Mortgage Brokers (NAMB) generally supported the inclusion of information listed on page 4 of the proposed GFE. However, NAMB objected to consolidating major categories on the GFE on the grounds that such categories tend to lead to consumer confusion since components are not evident to consumers until presented with the HUD-1, on which they are disclosed separately. NAMB also asserted that the proposed GFE is in conflict with the current RESPA requirements on affiliated business disclosure, because the proposed GFE eliminates the name of the provider on the GFE. NAMB submitted, in place of the proposed GFE, a model that provides symmetrical disclosure of originator compensation. NAMB stated that its model form not only remedies the disparity among originator disclosures, it more closely mirrors the HUD-1 than the proposed GFE; it does not create groupings of disclosures that must be broken out; and it is one page, making it more user friendly.

Other Commenters

Many other commenters also expressed concern about the length of the form. The National Association of Realtors (NAR) stated that the proposed GFE fails to achieve the

right balance between providing the necessary information and presenting such information simply in a manner to be useful to the consumer. NAR asserted that the disclosures, tables, and instructions in the proposed GFE will serve as a "psychological barrier" to many consumers who will feel overwhelmed with having to read, comprehend, and act on this amount of information. NAR stated that the decision not to include itemized costs in the proposed GFE will result in consumers getting less than the full disclosure Congress intended in the original statute. NAR asserted that the proposed GFE creates the opportunity to bury additional, undisclosed fees into "packages" and prevents individual provider cost comparison to the detriment of consumers.

NAR also recommended that the proposed GFE and the HUD-1 mirror each other in order to assist consumers in understanding whether the terms and expenses that were disclosed at loan application are those that are the governing terms at closing. NAR noted that, along with CRL, it previously recommended that HUD provide consumers a summary GFE accompanied by a full GFE with detailed explanations of each subcategory of fees to help consumers understand the services and fees for which they are being charged. NAR reiterated this recommendation for the final rule and, along with the American Land Title Association (ALTA), submitted a summary GFE and a full GFE for HUD's consideration.

The Credit Union National Association (CUNA) opposed increasing the GFE to the proposed four-page form. CUNA stated that the proposed form would not benefit borrowers who could be confused by the additional information, rather than helped in understanding their loan options. The National Association of Federal Credit Unions (NAFCU) stated that the length of the proposed form is too long for the purpose of the

GFE, which is simply to provide a good faith estimate of settlement costs. NAFCU recommended that pages 3 and 4 of the proposed form be consolidated into one page by removing the section on page 3 entitled "understanding which charges can change at settlement" and the section on page 4 entitled "using the shopping chart." NAFCU suggested that the information contained in these sections should be provided in the Special Information Booklet.

The Conference of State Bank Supervisors (CSBS), the American Association of Residential Mortgage Regulators (AARMR), and the National Association of Consumer Credit Administrators (NACCA) stated that they support HUD's goal to provide clear and valuable information to consumers regarding adjustable rate mortgages on the GFE. These commenters recommended that HUD work with the Federal Reserve Board to develop coordinated, consistent, and cooperative disclosures to ensure that consumers are not confused. They recommended that the GFE contain an estimate of taxes and insurance even when there will be no reserve for taxes and insurance in the monthly payment. According to these commenters, if the estimate is not included in the monthly payment amount, the borrower will not clearly understand whether they can afford the monthly payment. While these commenters indicated their general support for the grouping of fees and charges on the proposed GFE into major settlement cost categories, they expressed concern that some in the industry might take advantage of this format by putting additional fees and charges in a totaled category.

ALTA stated that page 1 of the proposed GFE presents the summary of loan terms and the total costs for settlement services in an understandable format. However, ALTA urged HUD to improve the individual fee disclosures by using a page that is identical to

page 2 of the current HUD-1. ALTA stated that revising page 2, as it recommended, would allow consumers to know all fees included within the total amount listed on the GFE summary page and to more directly compare these fees to the final charges and closing.

With respect to the categorization of fees on page 2 of the proposed GFE, ALTA objected to the proposed requirement that a single fee be disclosed for title services and lender's title insurance on Block 4 and for primary title services in the 1100 section of the HUD-1. ALTA stated that the elimination of required itemization of these fees is of concern and can only serve to lessen, rather than enhance, competition for these services.

ALTA asserted that HUD's views that consumers: (1) shop among lenders based on the lender's estimates of charges in the 1100 series on the HUD-1, and (2) have no need to know the amounts of the various charges that comprise the aggregate amount, are in error. ALTA stated that with regard to the itemization of individual costs that comprise the aggregate Block 4 charge, consumers who want to shop for these services will be seriously disadvantaged because there is no way to determine the lender's estimated price for the title company, escrow company, attorney, or surveyor.

ALTA also stated that the disclosure of a single fee for title insurance fails to recognize that, in most areas of the country, the seller generally pays a substantial portion of the title insurance charges. ALTA noted that the March 2008 proposed rule failed to provide instruction as to how to disclose title-related fees when these costs are paid by the seller. ALTA expressed concern that if the GFE and HUD-1 do not itemize the fees for title insurance services, the possibility exists that the borrower could pay for services for which sellers currently assume payment, and this would result in higher costs to the

borrower. ALTA requested that HUD continue to require title insurance fees disclosed in the 1100 series of the HUD-1 to be separately itemized on both the GFE and HUD-1.

With respect to the category for owner's title insurance on page 2 of the GFE, ALTA requested that the word "optional" be dropped from the disclosure on both the proposed GFE and the proposed HUD-1. ALTA expressed concern that, by including the word "optional" in both disclosures, HUD appears to be suggesting that a consumer does not need separate coverage for title insurance, which may discourage borrowers from obtaining owner's coverage. ALTA also noted that owner's title insurance is required in residential real estate transactions in many states and that, by labeling owner's title insurance as optional on both the GFE and the HUD-1, HUD's requirement would directly conflict with various state requirements.

Federal Agencies

The Federal Deposit Insurance Corporation (FDIC) also expressed concern about the length of the proposed GFE. While considering the proposed GFE to be an improvement over the current model form, the FDIC expressed concern about whether the proposed GFE provides information that consumers will understand in an easily understandable format. The FDIC also commented that more information about potential payment shock and the adjustment of interest rates should be included on the GFE. Specifically, the FDIC recommended that the GFE explain when an initial interest rate expires and when monthly payments increase.

The Federal Trade Commission (FTC) staff comment stated that the proposed GFE form offers several features that will benefit consumers. These features include a summary overview of loan terms and charges on the first page; the additional details

regarding categories of fees and shopping options on subsequent pages; and the focus on total settlement costs, rather than itemized costs. However, FTC staff stated that the form raises concerns that warrant clarification or modification. For example, FTC staff stated that consumers may be confused based on the differences between the GFE and the HUD-1 disclosures and the TILA forms they receive, particularly the difference in monthly amounts. Rather than explain the differences in the Special Information Booklet, FTC staff recommended that HUD provide a clear explanation of the difference between the forms on the GFE and the closing script, or use an alternative disclosure on the GFE and closing script to ensure as much consistency with the TILA disclosures as possible.

The Office of Thrift Supervision (OTS) commented that HUD should consider revising its settlement cost booklet to include illustrations reflecting the impact that loan features and terms can have on the cost of the mortgage. In particular, OTS stated that such illustrations would be particularly useful in reflecting payment shock, among other features, that a borrower may experience when rates reset.

HUD Determination

In response to comments, HUD has made a number of changes to the revised GFE, including shortening the form from four pages to three and clarifying important information for borrowers throughout the form. While HUD recognizes that too much information on the form may overwhelm borrowers, HUD is also cognizant that borrowers need to be aware of the important aspects of the loan, as well as the settlement costs. While HUD considered all of the various alternative forms submitted by commenters, HUD determined that its proposed GFE, with certain modifications made at

this final rule stage, would best meet the needs of borrowers to shop and compare loans from different loan originators. As demonstrated by the testing of the form conducted by HUD's forms contractor, consumers liked the general format of the form and were not overwhelmed by its length. Accordingly, HUD has maintained several important features of the proposed GFE in the final form. Other features from the proposed form have been removed from the form, as revised at this final rule stage, and will be included in the revised Special Information Booklet. The final GFE continues to inform borrowers about critical loan and settlement cost information and allows borrowers to effectively shop among loan originators without burdening them with extraneous information.

The top of page 1 of the revised form continues to include blank spaces for the loan originator's name, address, phone number, and email address, as well as the borrower's name, the property address, and the date of the GFE. In addition, the top of the revised page 1 includes a statement about the purpose of the GFE, and information on how to shop for a loan offer. This section of the form also references HUD's Special Information Booklet on settlement charges, as well as Truth in Lending disclosures and information available at www.hud.gov/respa. Such information was included on page 4 of the proposed form. While the revised page 1 also continues to include information about important dates, such as how long the interest rate is available and how long the estimate for all other settlement charges is available, the rate lock period information that was included in the loan summary chart on the proposed GFE has been moved from the summary chart to the "important dates" block on the revised form. This change was made to consolidate all the information about dates in one section of the form and to minimize potential borrower confusion.

The revised page 1 also includes a summary chart of the loan on which the GFE is based, but this section of the form is now referred to as "summary of your loan" instead of "summary of your loan terms," as proposed. The revised summary continues to include key terms and information about the loan for which the GFE was provided, but certain changes were made to headings on the chart to address specific comments. While the proposed GFE included information about the monthly escrow payment in the summary chart, the revised form includes a separate section concerning the escrow account. This section, referred to as "escrow account information," informs the borrower that some lenders require an escrow account to hold funds for paying property taxes or other property-related charges in addition to the monthly payment. The section includes a disclosure as to whether an escrow account is required for the loan described in the GFE. If no escrow account is included for the loan, this section informs the borrower that the additional charges must be paid directly when due. If the loan includes an escrow account, the section informs the borrower that it may or may not cover all additional charges.

The bottom of page 1 on the revised form retains the "summary of your settlement charges" section, as set forth in the proposed GFE. The summary includes the amount from Block A on page 2, "your adjusted origination charges"; the amount from Block B on page 2, "your charges for all other settlement services"; and reflects the "total estimated settlement charges" as the sum of Blocks A and B.

Page 2 of the revised GFE, like page 2 of the proposed form, contains a listing of estimated settlement charges. The top of the second page continues to require that the origination charge be listed, and the credit or charge for the specific interest rate is

required to be subtracted or added to the origination charge to arrive at the adjusted origination charge. However, this portion of the second page includes some minor changes from the proposed form. First, Block 2 now references "points" after the "charge" in the heading, rather than at the end of the sentence, to better inform the borrower. The heading now reads, "Your credit or charge (points) for the specific interest rate chosen." In addition, to draw the borrower's attention to the effect of the credit in Block 2, the term "reduces" is now bolded in box 2. To draw the borrower's attention to the effect of the charge in Block 2, the term "increases" is now bolded in box 3 of the second block. Finally, the second sentence in box 2 and box 3 in Block 2 refers to "settlement" charges rather than "upfront" charges, in order to be consistent with other language on the form.

Page 2 of the revised GFE, like the second page of the proposed GFE, also contains an estimate for all other settlement services. While the categories from the proposed form have generally been retained on the final form, certain changes have been made to the categories to streamline the form in response to comments. Block 10 of the proposed form "optional owner's title insurance" is now Block 5 of the revised form and informs the borrower that the borrower may purchase owner's title insurance to protect the borrower's interest in the property.

Block 6 of the revised form, "Required services that you can shop for," is the same as Block 5 of the proposed form. While Block 6 of the proposed form included both government recording charges and transfer taxes, in response to comments, government recording charges are now listed in Block 7 of the revised form, along with the explanation that "these charges are state and local fees to record your loan and title

documents." Block 8 now lists transfer taxes with the explanation that "these charges are state and local fees on mortgages and home sales." This change was made in response to comments so that these two different types of government fees could be treated differently with respect to tolerances, as explained below.

Block 7 of the proposed form, "Reserves or escrow," is now Block 9 of the revised form and is now listed as "initial deposit for your escrow account." The sentence below the title now explains that the charge is held in an escrow account to pay future recurring charges on the property and includes check boxes to indicate whether the escrow includes all property taxes, all insurance or other payments. The "other" category may include non-tax and non-insurance escrowed items, and/or specify which taxes or insurance payments are included in the escrow if the escrow does not include all such payments.

Block 8 of the proposed form, "Daily interest charges," is now Block 10 of the revised form. Block 9 of the proposed form, "Homeowner's insurance" is now Block 11 of the revised form.

The revised GFE requires the charges in Blocks 3 through 11 to be subtotaled at the bottom of page 2. The sum of the adjusted origination charges and the charges for all other settlement services are required to be listed on the bottom of page 2. This figure will also be listed on the bottom of page 1, in the block "Total Estimated Settlement Charges."

In light of comments received on various aspects of the proposed form, page 3 of the revised form has been redesigned to include the most important information from pages 3 and 4 of the proposed form. At the top of the redesigned page 3, the section

"Understanding which charges can change at settlement" includes information to assist the borrower in comparing charges on the GFE with the charges listed on the HUD-1 settlement statement. Next, the tradeoff table provides information on different loans for which the borrower is qualified that would increase or decrease settlement charges, with a corresponding change in the interest rate of the loan. Completing this tradeoff table is now optional. This table is intended to be read in conjunction with the section on "adjusted origination charges" on page 2 of the form. The tradeoff table on the final form has been modified to require "your initial loan amount" in the first category, as opposed to "your initial loan balance" on the proposed form, to be consistent with the change in terminology on the first page of the form.

Page 3 of the revised form also includes the shopping chart included on page 4 of the proposed form, to assist borrowers in comparing GFEs from different loan originators. Finally, the lender disclosure that was included on the proposed form has been retained on the revised form, as discussed below.

B. Changes to Facilitate Shopping

1. New Definitions for "GFE Application" and "Mortgage Application."

Proposed Rule. The March 2008 proposed rule provided separate definitions for a "GFE application" and a "mortgage application" in an effort to promote shopping. Under the proposed rule, a loan originator would have provided a borrower a GFE once the borrower provided the originator six pieces of information that included: borrower's name, Social Security Number, property address, gross monthly income, borrower's information on the house price or best estimate of the value of the property, and the amount of the mortgage loan sought. The rule provided that the GFE application would

have to be in written form and, if provided orally, would have to be reduced to a written or electronic record. Under the March 2008 proposed rule, a separate GFE would have to be provided for each loan where a transaction involved more than one mortgage loan.

The proposed rule would have required that once a borrower chose to proceed with a particular loan originator, the loan originator could require the borrower to provide additional information through a "mortgage application" in order to complete final underwriting. This additional information could be used to verify the GFE, and could include income and employment verification, property valuation, an updated credit analysis, and the borrower's assets and liabilities.

The March 2008 proposed rule provided that a borrower could be rejected at the GFE application stage if the loan originator determined that the borrower was not creditworthy. The borrower could not be rejected at the mortgage application stage unless the originator determined there was a change in the borrower's eligibility based on final underwriting, as compared to information developed for such application prior to the time the borrower chose the particular originator. Under the proposed rule, the originator would have been required to document the basis for such a determination and maintain the records for no less than 3 years after settlement.

The March 2008 proposed rule also provided that where a borrower was rejected for a loan for which a GFE had been issued, but the borrower qualified for a different loan program, the originator would have to provide a revised GFE. If a borrower was rejected for a loan and no other loan product could be offered, the borrower would have to be notified within one business day and the applicable notice requirements satisfied.

Under the March 2008 proposed rule, for loans covered by RESPA, the TILA disclosures would be provided within 3 days of a written GFE application, unless the creditor, i.e. the loan originator, determined that the application could not be approved on the terms requested. The proposed rule indicated that based on consultations with the Federal Reserve Board, when a GFE application is submitted, an initial TILA disclosure would also have to be provided, so long as the application was in writing, or, in the case of an oral application, committed to written or electronic form. HUD noted that whether a GFE application under a particular set of facts triggered the Home Mortgage Disclosure Act (HMDA) or the Equal Credit Opportunity Act (ECOA) requirements would be determined under Regulation B and Regulation C, as interpreted in the Federal Reserve Board's official staff commentary.

Comments

Consumer Representatives

Consumer representatives supported early delivery of the GFE, which, under the proposed rule, would be issued when a lender receives the proposed "GFE Application." However, they emphasized that enforcement and private rights of action are necessary to ensure that a meaningful GFE will be provided to consumers early in the mortgage application process.

Consumer representatives also raised the issue of whether HUD's definition of "GFE Application" triggers other regulatory requirements. They recognized the Federal Reserve Board's rulemaking authority under ECOA and the Fair Credit Reporting Act (FCRA) and indicated that requirements under these statutes and their implementing regulations would be triggered by the newly defined GFE application. They noted that

current definitions in both statutes and their implementing regulations cover the GFE application.

According to their comments, the application of ECOA and FCRA to the GFE application is important because such application ensures binding and accurate disclosures. These commenters recommended that HUD coordinate with the Federal Reserve Board to ensure that the GFE application remains covered by ECOA and FCRA.

Industry Representatives

Industry representatives expressed significant concerns about the "GFE Application" and "Mortgage Application" approach under the March 2008 RESPA proposal. Specifically, they expressed concerns about the limited information originators would be permitted to collect in order to conduct preliminary underwriting before issuing a GFE. One commenter stated that this limitation precludes an originator from considering, at the GFE application stage, important information that a lender currently collects early in the transaction in order to develop a GFE. Some of those additional items include loan product type sought, purpose of loan, and information to compute the loan-to-value ratio. The commenters claimed that limiting consideration of this type of information would make it difficult for originators to provide a meaningful GFE, because they would be unable to provide any reliable estimate of cost or determine a borrower's ability to repay the loan. They also stated that the inability to consider important underwriting information until the mortgage application stage would result in the issuance of more than one GFE. The net result, they concluded, would lead to borrower confusion and increased costs to the borrower.

Industry commenters also expressed further operational concerns related to the limitations on underwriting information at the GFE stage. They stated that the limitation on information that loan originators can take into consideration, in developing a GFE, would force lenders to develop systems that could underwrite based on very limited information. They further stated that the originator would not have sufficient information to determine the type of property the consumer is considering – such as whether the property is commercial, industrial, vacation, or residential – or the type of loan the consumer is considering, such as a purchase money loan, refinance, or home equity loan. They stated it is important for the lender to have this information because the lender may not engage in the kind of lending a consumer seeks.

In addition, industry commenters expressed confusion over whether a credit report was one of the six pieces of information they could collect as part of the GFE application, and requested that HUD provide clarification on this subject.

Industry representatives also requested that HUD permit borrowers to expedite the application process and proceed to the mortgage application stage, when the borrower so desires due to timing or other concerns.

Industry representatives stated that the new application definitions in the March 2008 proposed rule would present uncertainty in complying with other mortgage-related statutes and regulations. They commented that compliance with other statutes and regulations is triggered by a mortgage "application." Because HUD's proposal included both a "GFE Application" and a "Mortgage Application," they commented that it is not clear which one is the "application" for purposes of compliance with other regulations. In particular, lenders expressed concern with the possibility that the "GFE Application"

would trigger compliance obligations under FCRA, ECOA, HMDA, and the TILA requirements. They requested that ambiguities surrounding compliance with these statutes and other laws be addressed to provide clarity and mitigate litigation exposure. For example, one lender noted that to calculate the spread for high-cost loans under Regulation Z and many state predatory lending laws, the index used is based on the month in which the "application" for credit is received by the creditor. This lender stated that it was not clear from the proposed rule whether the GFE application is an application for purposes of Regulation Z.

Industry commenters expressed confusion about preamble statements regarding whether HMDA or ECOA is triggered by the GFE Application. They indicated that the preamble stated that whether HMDA or ECOA is triggered by the GFE Application should be determined under Regulations C and B, as interpreted by the Board. They noted, however, that the preamble stated that based on consultations with the Federal Reserve Board, TILA disclosures would be provided within 3 days of a written GFE application unless the creditor determines that the application cannot be approved on the terms requested. The commenters further noted that the Regulatory Impact Analysis states "[t]he proposed rule clarifies that only the mortgage application would be subject to Regulations B (ECOA) and C (HMDA), which is the current situation today." These commenters requested clarification of this matter.

Industry representatives questioned HUD's legal authority to: limit information originators can request to underwrite a loan; require that originators accept an abbreviated application from which to complete a GFE; require a new GFE when a counteroffer is

made; and require a consumer to be notified within one business day of a lender's decision to reject an application, among other concerns.

Additionally, one lender commented that under HUD's March 2008 proposed rule, lenders would be required to retain the GFE application for 3 years, which is different from the 25-month retention requirement by TILA or ECOA. The lender commented that this difference presents additional expense without a substantive benefit to the consumer.

Other Commenters

The FTC staff recommended that HUD reevaluate the proposed "GFE application," as this terminology is new and could generate consumer confusion in the already complex mortgage process. FTC staff suggested that HUD characterize it as the "GFE application" concept so that consumers do not confuse it with the mortgage application. They also recommended that HUD educate consumers about these two components of the mortgage lending process. Further, FTC indicated that the industry would also benefit from guidance on how the GFE application relates to other mortgage lending laws that include an "application" concept.

CSBS, AARMR, and NACCA also expressed concern over the creation of a "GFE application" and a "mortgage application" because, they asserted, these application concepts will cause consumer confusion. They recommended that HUD coordinate with other federal regulatory agencies to ensure consistency and clarity to regulatory requirements from loan application to loan closing.

HUD Determination

To address the concerns raised by the commenters about the bifurcated application approach set forth in the proposed rule, HUD has adopted a single application process for the final rule. Under this approach, at the time of application, the loan originator will decide what application information it needs to collect from a borrower, and which of that collected application information it will use, in order to issue a meaningful GFE. However, before providing the GFE, the loan originator will be assumed to have collected at least the following six items of information: the borrower's name, Social Security Number, and gross monthly income; the property address; an estimate of the value of the property; and the amount of the mortgage loan sought. The borrower's Social Security Number would be collected for purposes of obtaining a credit report. The final rule now defines "application" to include at least these six items of information. Therefore, under this single application process, a loan originator may ask for, or a borrower may choose to submit, more information than the loan originator intends to use to process the GFE, for example the information on a standard 1003 mortgage loan application form, but beyond the six items of information, the loan originator will determine what it needs to issue a GFE. HUD strongly urges loan originators to develop consistent policies or procedures concerning what information it will require to minimize delays in issuing GFEs.

In order to prevent overburdensome documentation demands on mortgage applicants, and to facilitate shopping by borrowers, the final rule specifically prohibits the loan originator from requiring an applicant, as a condition for providing a GFE, to submit supplemental documentation to verify the information provided by the applicant on the application. Loan originators, however, can require applicants to provide such

verification information after the GFE has been provided, in order to complete final underwriting. In addition, the rule does not bar a loan originator from using its own sources before issuing a GFE to independently verify the information provided by the applicant.

Once the applicant submits to the loan originator all the mortgage application information deemed necessary by the loan originator to process the GFE, the originator will be required to deliver or mail a GFE to the applicant within 3 business days. HUD is now also limiting the fee that may be charged for providing the GFE, consistent with the Federal Reserve Board's recently finalized rule limiting the fees that consumers can be charged for the delivery of TILA disclosures (see revisions of 12 CFR 226.119(a), 73 FR 44522, July 30, 2008).

After the GFE has been received, the loan originator may collect additional fees needed to proceed to final underwriting for borrowers who decide to proceed with a loan from that originator. As noted, at that time, verification information or any other information could be required from the applicant, such as bank statements and W-2 forms, to confirm representations made by the applicant in the application.

None of the information collected by the originator prior to issuing the GFE may later become the basis for a "changed circumstance" upon which a loan originator may offer a revised GFE, unless the loan originator can demonstrate that there was a change in the particular information or that it was inaccurate, or that the loan originator did not rely on that particular information in issuing the GFE. A loan originator would have the burden of demonstrating nonreliance on the collected information, but may do so by various means, including through, for example, a documented record in the underwriting

file or an established policy of relying on a more limited set of information in providing GFEs. If a loan originator issues a revised GFE based on information previously collected in issuing the original GFE and "changed circumstances," it must document the reasons for issuing the revised GFE, including, for example, its nonreliance on that information or the inaccuracy of the information, and retain that documentation for at least 3 years. Additional guidance on what constitutes "changed circumstances" will be provided by HUD during the implementation period.

Furthermore, the loan originator is presumed to have relied on the borrower's name, the borrower's monthly income, the property address, an estimate of the value of the property, the mortgage loan amount sought, and any information contained in any credit report obtained by the loan originator before providing the GFE. The loan originator cannot base a revision of the GFE on this information, unless it changes or is later found to be inaccurate. HUD determined that this approach provides the flexibility originators need to properly underwrite, while limiting bait-and-switch methods whereby the originator uses the GFE to draw in a borrower and, after a significant application fee is paid or burdensome documentation demands are made, claims that a material change has resulted in a more expensive loan offering.

If a loan originator receives information indicating that changed circumstances necessitate the issuance of a new GFE, such new GFE must be provided to the borrower within 3 business days of receipt of such information. The 3-day requirement is in response to comments on the proposed rule that stated that providing a new GFE within one day is not workable.

The approach set forth in this rule furthers HUD's goal to promote consumer shopping among mortgage originators, because it does not overly burden a consumer at an early stage. Rather, a consumer provides information that is easily communicated and pays a nominal fee in order to get a GFE.

As noted, this public policy is further supported by the Federal Reserve Board through its recently issued final rule limiting fees that can be charged for the delivery of the TILA disclosure. Under this rule, borrowers must receive the TILA disclosure before paying or incurring any fee imposed by a creditor or other person in connection with the consumer's application for a closed-end mortgage, except that creditors may charge a bona fide and reasonable fee for obtaining the consumer's credit history. Whether an application under a particular set of facts triggers ECOA or HMDA requirements must be determined under Regulation B or Regulation C, as interpreted by the Federal Reserve Board's Official Staff Commentary.

2. Up-Front Fees that Impede Shopping.

Proposed Rule. The March 2008 proposed rule provided that a loan originator, at its option, could collect a fee limited to the cost of providing the GFE, including the cost of an initial credit report, as a condition of providing the GFE to a prospective borrower. The loan originator was not permitted to collect, as a condition of providing a GFE, any fee for an appraisal, inspection, or other similar service needed for final underwriting.

Comments

Consumer Representatives

Consumer representatives expressed concerns about the opportunity for consumers to be charged a fee for a GFE and a credit report. They are concerned such costs would discourage borrowers from shopping for a mortgage. They stated that lenders would charge a fee for the GFE to offset lenders' costs for issuing the GFE, because the cost of preparation of the GFE cannot otherwise be passed on to consumers. Consumer advocates pointed out that some states prohibit the collection of an application fee before credit has been extended and that HUD's proposal would be inconsistent with such laws. The consumer advocates asserted that HUD's proposal could be read to preempt these state laws. The consumer advocates recommended that HUD remain silent on the collection of such fees in relation to the GFE and should in no way support it.

Industry Representatives

Industry comments reflected some confusion as to whether and to what extent fees can be charged in connection with the GFE. Some industry commenters understood the proposal to mean that lenders can charge a fee once a borrower submits a "mortgage application." Other industry commenters sought clarification about what exactly can be charged in connection with the GFE. They indicated that meeting the 3-business day requirement for delivery of the GFE to the borrower and completing the lengthy GFE form would be time consuming and costly.

Further, in a situation in which a borrower seeks an accelerated process for getting a loan, industry representatives stated that the borrower should be able to pay necessary fees for such items as, for example, an appraisal. Industry representatives also opined that under RESPA, HUD has no authority in their view to require lenders to offer GFEs without adequate compensation.

Other Commenters

CSBS, AARMR, and NACCA commented that a consumer should not be charged for the GFE because to do so locks the consumer into the transaction. These commenters stated that if HUD insists on permitting a fee to be charged, the fee charged should be limited to a credit report.

HUD Determination

HUD has long supported a public policy goal of creating a circumstance where consumers can shop for a mortgage loan among loan originators without paying significant upfront fees that impede shopping. To this end, and consistent with the Federal Reserve Board's recently issued revised regulations limiting the fees that a consumer may be charged for the delivery of TILA disclosures (73 FR 44522, July 30, 2008), HUD, in this final rule, is limiting the charge originators may impose on consumers for delivery of the GFE.

The Federal Reserve Board's rule restricts creditors from imposing a fee on a consumer in connection with the consumer's application for a mortgage before the consumer has received the TILA disclosure. The Federal Reserve Board makes an exception that allows imposition of a fee that is bona fide and reasonable in amount for obtaining the consumer's credit history. In an effort to create consistency among regulatory requirements and serve the best interests of consumers, HUD is similarly limiting the fee for the GFE to the cost of a credit report. Also, as in the proposed rule, a loan originator is expressly not permitted to charge, as a condition of providing a GFE, any fee for an appraisal, inspection, or similar settlement service.

3. Introductory Language on the GFE Form.

Proposed Rule. The March 2008 proposed rule included a proposed required GFE form that explained to the borrower: (1) on page 1, the purpose of the GFE, i.e., that it is an "* * * estimate of your settlement costs and loan terms if you are approved for this loan"; and (2) on page 3, that the borrower is the " * * * only one who can shop for the best loan for you. You should shop and compare this GFE with other loan offers. By comparing loan offers, you can shop for the best loan."

Comments

Consumers did not comment on this issue. NAMB stated that the introductory language of the GFE and the language encouraging comparative shopping should be improved. Specifically, NAMB stated that the language encouraging comparative shopping incorrectly characterizes the GFE as a "loan offer." NAMB stated that this is misleading because it leaves borrowers with the impression that they have been approved for the loan and that is not the case. NAMB suggested that the "loan offer" reference be changed to "other estimates."

NAMB also recommended that the language encouraging comparative shopping be made more conspicuous and informative. NAMB encouraged HUD to adopt language set forth in the prototype disclosure forms developed by FTC. Those forms include prominent legends in large typeface that expressly advise borrowers that mortgage originators, including both brokers and lenders, do not represent borrowers, and that the "lender or broker providing this loan is not necessarily shopping on your behalf or providing you with the lowest cost loan." The FTC prototype forms also encourage borrowers to comparison shop to find the best deal.

NAMB urged HUD to adopt the FTC prototype disclosures in place of the proposed mortgage broker compensation language. However, NAMB recommended that, if the FTC forms are not adopted in their entirety, HUD should incorporate the FTC language in the GFE earlier than on page 3, and in a more prominent typeface than the typeface used for the proposed language on comparative shopping.

HUD Determination

HUD's consumer testing of the form demonstrated that consumers better understood the function of the GFE and its role in the shopping process as a result of language on the form. Accordingly, HUD has determined to maintain the language on the form that describes the purpose of the GFE and informs the borrower that only they can shop for the best loan for them. However, in the interest of streamlining the form, the revised form now includes, on page 1, the information about shopping for a loan that was on page 3 of the proposed GFE.

4. Terms on the GFE (Summary of Loan Details)

Proposed Rule. The proposed GFE included a summary of the key loan terms. The form required the disclosure of the initial loan amount; the loan term; the initial interest rate on the loan; the initial monthly payment owed for principal, interest, and any mortgage insurance; and the rate lock period. The form also required the loan originator to disclose whether the interest rate could rise; whether the loan balance could rise; whether the monthly amount owed for principal, interest, and any mortgage insurance could rise; whether the loan had a prepayment penalty or a balloon payment; and whether the loan included a monthly escrow payment for property taxes and possibly other obligations. The proposed rule required the terms "prepayment penalty" and "balloon

payment" to be interpreted consistent with TILA (15 U.S.C. 1601 et seq.). The APR was not included on the proposed GFE.

Comments

Consumer Representatives

As part of their general support for the proposed rule, consumer advocacy organizations were positive about the inclusion of loan terms on the GFE. NCLC, in a joint letter with Consumer Action, Consumer Federation of America, and National Association of Consumer Advocates, commented that "[p]lacing the most critical information in consumers' hands in a consistent, user-friendly format should facilitate consumer shopping, market competition and transparency." They characterized HUD's summary sheet as striking a balance between disclosing critical information and preventing information overload.

CRL presented a legal argument supporting HUD's authority to require disclosure of loan terms. CRL pointed out that settlement costs are so intertwined with loan terms that those terms must be disclosed for the settlement costs to have any meaning. Other consumer groups also pointed out that these terms affect the overall price and risk for the consumer. CRL, which is affiliated with a small nonprofit lender that will have to comply with the new rule, stated that the rule is administratively feasible for larger and smaller lenders.

In addition to supporting loan terms disclosure, consumer advocacy organizations suggested several changes to make disclosure even more effective. They suggested that there should be a more strict legal mechanism for binding originators to the loan terms after disclosing them. Some consumer advocates argued for inclusion of the APR on the

GFE, perhaps instead of the note rate, stating that inclusion of the APR would make comparisons easier. Some suggested that the adjustable rate disclosure should include the date when the first adjustment happens, in order to help avoid payment shock. Commenters pointed out that a monthly payment disclosure that includes taxes and different types of insurance will be more useful in judging affordability and for making comparisons to the current mortgage, when applying to refinance. They also suggested that the maximum interest rate disclosure is not likely to help borrowers and may be misleading. The commenters stated that actual dollar figures are more readily understandable. The commenters also stated that the GFE should include a clear statement that loan terms are negotiable, and all the disclosures should be more carefully harmonized with TILA.

NCLC, Consumer Action, the Consumer Federation of America, and the National Association of Consumer Advocates stated that they "applaud" inclusion of the maximum payment amount and the maximum loan balance because these help consumers understand a loan's risks, especially the risks of nontraditional loans, and help consumers judge a loan's affordability. However, these organizations suggested that HUD provide guidance to originators on how to calculate maximum payment and maximum loan balance.

One consumer organization pointed out that much research, including an FTC study, found that borrowers often do not understand exactly what "prepayment penalties" are and how they work. Therefore, the organization recommended that HUD include in the prepayment penalty disclosure the following brief explanation: "[p]ayment to lender if you refinance, sell home, or pay your loan off early".

Consumer groups were concerned that, because the proposed GFE highlighted settlement costs, it might mislead borrowers into believing that interest costs are less important. They suggested that interest is usually much more expensive than closing costs, and should be more effectively emphasized.

Industry Representatives

Most lenders and lender organizations urged that loan terms be left off the GFE, submitting that loan terms are more properly viewed as TILA disclosures. These commenters stated that double disclosure of loan terms will be confusing to borrowers, especially since much of the terminology proposed to be used in HUD's GFE is different from that used in the TILA (e.g., "loan amount" vs. "amount financed") and some calculations are different. These organizations suggested that loan term disclosures should be coordinated with TILA, and be less lengthy. A lender proposed that originators should be allowed to substitute early TILA disclosure for the loan terms sheet. Another lender organization stated that loan terms should be included only if there is a combined RESPA/TILA form. Some credit unions stated that the APR should be included in the GFE loan terms.

Some lenders stated other aspects of the loan terms disclosure would confuse borrowers. A lender organization suggested that use of the format "Your … is" to describe the loan details would create misunderstanding, because these were loan terms being applied for, not final loan terms. The same organization also believed that inclusion of mortgage insurance in the monthly payment, without disclosing whether mortgage insurance is required, would confuse borrowers. In addition, the organization

stated that some of the mechanisms behind these loan terms are too complex for single-line disclosure.

Many lenders and lender organizations submitted that HUD has no authority under RESPA to require disclosure of loan terms, because loan terms are not part of the settlement process. These lenders submitted that HUD has the authority to require disclosure of settlement costs only, and that loan terms are not settlement costs. They stated that the disclosures required by HUD would overlap or conflict with disclosures under TILA and potentially with ECOA and HMDA. One lender also stated that some of these disclosures would overlap with state-mandated disclosures.

Industry representatives commented that the Federal Reserve Board and lenders have experience and expertise in developing disclosures and informational materials on adjustable rate mortgages, and that HUD should coordinate efforts to provide improved disclosures and informational materials. Industry commenters also stated that disclosures related to ARMs give rise to different concerns than settlement costs under RESPA and that HUD should follow the Federal Reserve Board's lead in this respect. A lender stated that the rate adjustment disclosure on the proposed GFE is biased against ARMs, since it only shows that payments can increase, not decrease. This same lender suggested that it would be better to have full ARM disclosure, which industry needs because current ARM disclosures are inadequate.

NAMB supported HUD's inclusion of loan terms on the GFE, and suggested that more monthly expenses should be disclosed, such as homeowner's association dues, if applicable.

The Mortgage Insurance Companies of America (MICA) objected to the fact that mortgage insurance costs were included in the monthly payment for purposes of the question, "Can your monthly amount owed for principal, interest, and any mortgage insurance rise?" MICA commented that this disclosure may mislead borrowers into believing that their mortgage insurance payments can rise, when they are in fact set at the time of origination. MICA also suggested that mortgage insurance would be disclosed in the "Required services that the loan originator selects" category, and would also be included in the escrow disclosure.

Other Commenters

CSBS, AARMR, and NACCA commented that HUD should be aware that several states already require loan originators to disclose various loan terms, and that the GFE should avoid conflicting with these requirements. This group also suggested that, in order to avoid consumer confusion, HUD should coordinate more closely with the Federal Reserve Board's TILA disclosures.

Federal Agencies

FTC staff stated that its experience and research suggest that "consumers in both the prime and subprime markets would benefit most from the development of a single mortgage disclosure document that consolidates information on the key costs and features of their loans, presents the information in a language and format that is easy to understand, and is provided early in the transaction to aid consumer shopping." However, FTC staff stated their belief that HUD's GFE did not go far enough in requiring these disclosures, and that even the GFE and the TILA form together did not

disclose the necessary information. FTC staff also stated that inconsistencies between the GFE and TILA forms could lead to consumer confusion.

The FDIC commended HUD for proposing revisions to its RESPA regulations, and stated that "[t]he earlier availability of and more relevant information on the GFE should promote comparative shopping that will enable consumers to make more informed financing decisions." Like the consumer organizations, the FDIC expressed its view that the GFE needs to include disclosure of when the first interest rate adjustment happens, in order to avoid payment shock.

The Federal Reserve Board staff agreed with the need for disclosure of the first rate adjustment, and stated that because the GFE's ARM disclosures are less complete than TILA disclosures, the GFE's ARM disclosures may not be as beneficial to consumers' understanding of how their loans work. The Federal Reserve Board staff's main concern, though, was that duplication of disclosures and information, and, in some instances, inconsistency between the loan terms on the GFE and the TILA form will create confusion for consumers. The Federal Reserve Board staff suggested that because RESPA and TILA overlap, the Federal Reserve Board and HUD should work together to develop a single RESPA/TILA form. In addition, the Federal Reserve Board staff stated, similar to a consumer organization comment, that the absence of taxes and insurance in the monthly payment disclosure will interfere with borrowers' ability to gauge affordability.

HUD Determination

After reviewing the comments, HUD continues to believe that consumer understanding of mortgage loans and of their settlement costs will be greatly enhanced by

requiring disclosure of certain loan terms in a clear, user-friendly format on the GFE. Therefore, the final rule includes the proposed loan summary chart on the first page of the revised GFE, with some revisions to address commenters' suggestions. To fully understand the cost of a loan for which a borrower is paying, the borrower needs to know the terms of the loan product. Loan terms, such as the interest rate, can have a direct relationship to the borrower's settlement costs, including mortgage broker compensation and other loan origination charges. HUD has emphasized the importance of disclosing the relationship between the interest rate and settlement charges in statements of policy on mortgage broker compensation and past RESPA rulemaking efforts. Disclosure of this relationship continues to be a central element of this rule.

Making it easier to understand the relationship between loan terms and loan costs is a key element in enhancing a borrower's ability to shop for the best-priced loan, including settlement charges. A borrower should know that a loan may have certain features -- for example, a prepayment penalty or a balloon payment -- that may affect the borrower's charges for that loan, including by affecting the mortgage broker's indirect compensation or other, direct loan origination charges. The new GFE brings together all of the relevant pricing information, including certain loan terms, on one form, thus allowing the consumer to understand and compare loans much more easily. As stated by the National Consumer Law Center, in its comment on behalf of itself, Consumer Action, the Consumer Federation of America, and the National Association of Consumer Advocates:

> "Using a loan summary sheet is a terrific advance. As HUD recognizes, consumer shopping is facilitated when loan information is condensed and

summarized. Placing the most critical information in consumers' hands in a consistent, user friendly format should facilitate consumer shopping, market competition, and transparency."

HUD has determined that disclosure of major loan terms on the GFE is necessary to provide effective advanced disclosure to homebuyers of settlement costs, which is a key purpose of RESPA. HUD disagrees with those industry commenters that asserted that the GFE cannot list loan terms associated with settlement costs because the TILA disclosure is the appropriate form for loan terms. The Federal Reserve Board, in its comment on the rule, noted an "overlap" between the RESPA and TILA's purposes in this regard: "Although RESPA's purpose is to inform consumers about settlement costs, and TILA's is to inform consumers about loan terms, these purposes overlap. Settlement costs may include loan origination fees, and consumers may finance their settlement costs." Under section 19(a) of RESPA, the Secretary of HUD has the authority to issue such regulations "as may be necessary to achieve the purposes of this Act." The added information provided by the new GFE clearly furthers RESPA's purpose to "provide more effective advance disclosure to homebuyers and sellers of settlement costs." HUD agrees with those commenters who asserted that disclosure of other settlement costs is meaningless (and therefore ineffective), absent the context provided by simultaneous disclosure of some loan terms. More effective disclosure also leads to, through borrowers' improved ability to shop for mortgages, reduced mortgage settlement costs for borrowers, a key purpose behind RESPA. HUD believes its new GFE, and its enhanced usefulness to borrowers as a shopping document, will provide an effective complement to

the TILA disclosure, to provide borrowers with a more complete picture of their mortgage loans.

Some commenters, primarily industry, requested that HUD delay its disclosure reform efforts in this rulemaking, pending a joint effort at disclosure reform with the Federal Reserve Board. HUD remains ready to coordinate with the Federal Reserve Board to ensure consistency in mortgage disclosure forms. As discussed earlier in this preamble, however, HUD determined that it must move forward with this rulemaking to provide prospective homebuyers and other mortgage borrowers the benefits of the better disclosure provided by the revised forms and requirements in this rule. These revisions are particularly important given the current mortgage crisis, which is due in part to borrowers' misunderstanding or lack of knowledge about the fundamental details of their mortgage loans.

HUD also examined the comments regarding its authority to require disclosure of loan terms on the GFE, and concludes that it does have such authority. Section 5(c) of RESPA provides for "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." Because, under RESPA's definitions, loan origination, or the making of a mortgage loan, is a "settlement service," HUD determined that it is within its authority to require that a good faith estimate of the costs associated with this specific settlement service include key information about the "specific" service. Without this information, the origination charges and other fees associated with the loan will be meaningless. Through RESPA, Congress entrusts HUD with establishing the contents of the GFE, and it is within HUD's discretion, and its responsibilities under RESPA, to

ensure that consumers receive enough information to make intelligent shopping decisions about the costs of their loans. As noted previously in this preamble, given the current problems in the mortgage market, HUD decided to move forward with its improved mortgage disclosures, including this new first page of the GFE. The CRL, in its comment on the 2008 proposed rule, stated:

> "In today's mortgage market, settlement costs are so intertwined with loan terms, and the illusory trade-off between rate and points is so problematic … loan terms simply must be included for the disclosure of settlement costs to be even remotely effective. HUD's authority to require them, therefore, is unambiguous."

In response to comments, HUD has revised several aspects of the loan summary chart on page 1 of the GFE, to better inform borrowers of the key loan terms. First, the title of this section of the GFE has been simplified to "Summary of your loan." To improve clarity, the summary chart now refers to "initial loan amount" instead of "initial loan balance." As in the proposed rule, the revised form requires disclosure of the terms of the loan; initial interest rate; and initial amount owed for principal, interest, and any mortgage insurance. However, the information on the rate lock period has been moved out of this section of the GFE and into the "Important dates" section.

While some commenters recommended that the "annual percentage rate" or "APR" be added to the summary chart, HUD has determined not to add "APR" to the GFE. HUD recognizes that APR is a complex term, calculated without the inclusion of certain significant costs in a mortgage loan transaction, and has a unique purpose as a broad cost-of-credit measure central to the TILA disclosure. Consumers will be apprised of the APR on the TILA disclosure they receive at the same time that they receive the

GFE. Accordingly, due to the specific TILA purposes of the APR and its inclusion on the concurrent TILA disclosure, HUD does not believe it is necessary to include the APR on the GFE.

HUD has, however, included on the GFE form other terms that are included in the TILA disclosure required by the Federal Reserve Board, but that are important to borrowers' understanding the costs of their mortgage loans. For example, the GFE requires a general disclosure about the existence of prepayment penalties and balloon payments. Under the final rule, HUD would continue to interpret these terms consistent with TILA, as HUD had indicated it would do in its March 2008 proposed rule (73 FR at 14036).

Some commenters recommended that the form warn borrowers about the first change in the interest rate, to prevent payment shock. The revised form requires disclosure of the length of time before that first change. In addition, the revised form clarifies whether, even when the borrower makes payments on time, the loan balance can rise and the monthly amount owed for principal, interest, and any mortgage insurance can rise. The revised form also requires disclosure of the period of time of the first possible increase in the monthly amount owed, the amount to which it can rise at that time, and the maximum to which it can ever rise. The final rule requires the same information as in the proposed form about prepayment penalties and balloon payments. Finally, the final rule, with some revision of the proposed rule language, requires information on whether the lender requires an escrow account for the loan, for the payment of property taxes and possibly other obligations.

5. Period during which the GFE Terms Are Available to the Borrower.

Proposed Rule. Under the proposed rule, the interest rate stated on the GFE would be available until a date set by the loan originator for the loan. After that date, the interest rate, some of the loan originator charges, the per diem interest, and the monthly payment estimate for the loan could change until the interest rate is locked. The proposed rule also provided that the estimate for all the other charges would be available until 10 business days from when the GFE is provided, but could remain available longer, if the loan originator extended the period of availability.

Comments

Consumer Representatives

NCRC, CRL, and NCLC all stated that a 10-business-day time period is insufficient for shopping and recommended a 30-day binding period as more fair to consumers. NCLC stated that the 10-business day period does not seem to be sufficient time for consumers to shop for a different mortgage, obtain alternative GFEs, compare them, and then make a decision to return to a particular originator, particularly without an interest rate lock. NCLC noted that industry practice generally assumes that, in the purchase money context, a minimum of 30 days is needed to shop for and obtain a binding mortgage commitment.

CRL also noted that the 10-business-day period does not apply to the interest rate, which can come with no guarantee at all. NCLC and CRL stated that an interest rate lock must be required in order for the GFE to be effective. According to CRL, not including a requirement for an interest rate lock will force consumers to shop on settlement costs alone, which are a relatively small component of the total home settlement cost. CLR stated that, in addition, not requiring a rate lock makes it too easy for loan originators to

engage in baiting and switching; that is, offering low settlement costs, only to recoup those costs by increasing the interest rate when the consumer returns 3 business days later. NCLC stated that, because interest is the largest component of the price of a mortgage, if interest rates are allowed to float, while settlement costs are fixed, consumers will be encouraged to shop on the smallest portion of mortgage costs, the settlement costs, and that lenders will be encouraged to play bait and switch games with the offered interest rate. Thus, according to NCLC, in order for the GFE to be an effective shopping tool, all costs must be fixed at the time the GFE is delivered.

Industry Representatives

MBA stated that the information concerning how long the costs and interest rate are open to borrower acceptance needs greater clarification and could be provided in accompanying materials, and not the GFE. MBA stated that if such information is included on the GFE, the rule should make clear that the interest rate on the GFE may be available until a specified hour and date, since interest rates frequently change several times a day.

The Consumer Mortgage Coalition (CMC) stated that RESPA already provides for good faith estimates of closing costs, and that it is unreasonable to interpret RESPA to limit changes in closing costs where the estimates were made in good faith. In addition, according to CMC, nothing in RESPA would appear to justify requiring lenders to keep an interest rate available for a potential borrower who has not actually applied for a loan. Therefore, CMC recommended that the “important dates” section on the proposed GFE be removed.

NAMB stated that it is meaningless, and potentially misleading, to suggest that a borrower would receive a specific interest rate prior to final application. NAMB recommended that more specific language be included on the form indicating that the rate may change until locked. They also recommended that the 10-business-day period during which estimated settlement charges would be available, be changed to 10 "calendar" days, since this would conform more closely to market realities.

HUD Determination

HUD has determined to retain the time periods set forth in the proposed rule. A central purpose of RESPA regulatory reform is to facilitate shopping in order to lower settlement costs, and there is legitimate concern that requiring GFEs to be open for too long a shopping period could unintentionally operate to increase borrower costs. This could occur if loan originators are required to commit to prices for too long a period or if the length of the period necessitates that originators make contingency plans for a large number of loans, when the yield of actual borrowers that can be expected to commit to the originator is uncertain. Accordingly, the final rule provides that the interest rate stated on the GFE will be available until a date set by the loan originator for the loan. HUD is not requiring the interest rate to be available for any specific length of time. The final rule provides that the loan originator indicate on the GFE the period during which the interest rate is available. After that time period, the interest rate, the interest rate related charges, and loan terms, including some of the loan originator charges, the per diem interest, and the monthly payment estimate for the loan could change until the interest rate is locked. The final rule also provides that the estimate for all other settlement charges and loan terms must be available for 10 business days from when the

GFE is provided, but could remain available longer if the loan originator chooses to extend the period of availability. The 10-business day requirement for settlement costs essentially provides that the GFE will be available for 2 weeks, thereby providing borrowers with sufficient time to shop among various providers.

6. Option to Pay Settlement Costs

Proposed Rule. The proposed GFE advised the borrower regarding how the interest rate would affect a borrower's settlement costs. The proposed GFE would have required the loan originator to complete a tradeoff table that informed the borrower that the borrower could choose from among the following: (1) the loan presented in the GFE; (2) an otherwise identical loan with a lower interest rate and monthly payments that will raise settlement costs by a specific amount; or (3) an otherwise identical loan with a higher interest rate and monthly payments that will lower settlement costs by a specific amount. If a higher or lower interest rate was not in fact available from the originator, the originator would have been required to provide those options that are available and indicate "not available" on the form, for those options that were not available. The proposed rule invited comments on whether the loan originator should be required to include a "no cost loan" on the tradeoff table as one of the alternative loans if the loan offered to the borrower is not the loan for which the GFE is written.

Comments

Consumer Representatives

Consumer representatives supported the concept of the tradeoff table but recommended some changes. They stated that only loans for which the borrower actually qualifies should be included in the table. They also stated that shopping on monthly

payments through the tradeoff table, proposed in HUD's RESPA rule, only works if the loan terms are the same. If loan terms vary, shopping on the monthly payment can be misleading to consumers and have devastating results. These commenters also expressed concerns about the definition of "otherwise identical," which anticipates that the loans offered on the tradeoff chart would vary only by interest rate. As outlined by these commenters, the problem is that if the lender pays the closing costs, the interest rate will be higher, and, if the borrower pays the closing costs, in many cases, the borrower will finance such costs through a higher loan amount. The commenters stated that the tradeoff table would not address this circumstance.

These commenters also recommend that the definition of "otherwise identical" be clarified, to include loans where the number and schedule of payments, the nature of the interest rate, whether fixed or adjustable, the index and margin for any adjustable rate mortgage, and the other loan characteristics, are held constant, with the exception that the interest rate and loan amount can be lower or higher than the loan reflected in the GFE.

Consumer representatives also expressed concerns that the introductory language on the tradeoff table implies that there is a one-to-one relationship between the interest rate and the settlement costs. They stated this is not the case, and, in many circumstances, the lender-paid broker compensation leads to both higher settlement charges and higher interest rates. In addition, they stated that the tradeoff table cannot effectively disclose the tradeoffs when lender-paid broker compensation is based on loan features other than an increase in the interest rate; as for example, lenders that commonly pay brokers for loans with prepayment penalties.

Some consumer representatives expressed support for a requirement that an originator be required to offer a no-cost loan on the tradeoff table if the originator has that type of product available and the borrower qualifies for such a loan. These commenters also stated that a meaningful tradeoff between settlement charges and interest rates would arise in the context of a no-cost loan.

Industry Representatives.

Industry representatives recommended that the tradeoff table on page 3 of the GFE be moved to explanatory materials, including the special information booklet. One lender expressed confusion over what HUD intended by "two other options." The lender stated that it was not clear whether HUD meant different loan types, rate/point structures, down payment amounts, or something else. A major lender trade organization commented that lenders should not be required to offer a no-cost loan on the tradeoff table. A major lender stated that since HUD has not defined what it means by "no cost," it is difficult to provide a comment. This lender stated that many lenders now offer no-cost loan products and to force these lenders into making such disclosures would only result in consumer confusion.

One lender commented that disclosing two mortgage products on the tradeoff table, in addition to the product contemplated on the GFE, would be problematic, because this particular lender offers only two mortgage products.

Other Commenters

CSBS, AARMR and NACCA commented that the tradeoff table does not disclose that the choice a borrower makes between a charge and a credit will have an impact on

the overall amount of the loan or monthly payment. The disclosure should reflect such a choice.

HUD Determination

HUD has determined to retain the tradeoff table on the GFE. However, recognizing that not all loan originators offer various loan products, full completion of the table is at the option of the loan originator. While a loan originator is required to complete the left hand column of the table that describes the loan offered in the GFE, it is not required to complete the table with respect to the middle column reflecting a loan with a lower interest rate, or the right hand column, reflecting a loan with lower settlement charges. Filling out these last two columns is optional for the loan originator, even if the loan originator has another loan for which the borrower may be eligible. However, HUD encourages loan originators to complete the tradeoff table, in light of HUD's consumer testing of the form that revealed that consumers found the tradeoff table to be one of the most useful and informative aspects of the GFE. The tradeoff table focuses consumers' attention on the information in the box on the top of page 2 of the GFE, empowering them to better shop for a mortgage. HUD strongly urges loan originators to fill out the tradeoff table in its entirety so that borrowers can better understand: (1) the disclosure of the "charge or credit (points) for the specific interest rate chosen" on page 2 of the GFE, and (2) what other loans may be available.

As many commenters expressed concern and confusion over the requirement to provide information about alternative loans and about "otherwise identical" loans, HUD is clarifying the scope of what qualifies as an "otherwise identical" loan. Should a loan originator determine to complete the table, the loan originator has to disclose only those

loans for which the borrower would qualify under the lender's underwriting practices. For purposes of completing the tradeoff table, an "otherwise identical" loan is a loan where the loan amount, the number and schedule of payments, the nature of the interest rate, the index and margin for any adjustable rate mortgage, the loan terms, and characteristics such as whether there is a prepayment penalty or a balloon payment are consistent with the loan presented in the GFE. The only loan characteristic that may vary from the loan presented in the GFE is the interest rate.

No-cost loans are not required to be presented as one of the alternative loans. However, if the baseline GFE is for a no-cost loan so that the origination charge in Box 1 or the credit shown in Box 2 of the GFE offset the total of other settlement service charges in Boxes 3 through 11 (i.e., total estimated settlement costs are zero), the originator would complete the tradeoff table by showing the same loan amount with positive closing costs (effectively the positive difference between the charge or credit for the GFE interest rate and that for the specified lower interest rate) as the first alternative to the GFE loan, and the same loan with a higher interest rate and negative closing costs (effectively the negative difference between the charge or credit for the GFE interest rate and that for the specified lower interest rate) as the second alternative. The primary purpose of the GFE tradeoff table is to ensure that borrowers understand there is a trade off between interest rates and settlement costs and to help them better understand the "Your credit or charge (points) for the specific interest rate" disclosure on page 2. It may also help borrowers become aware of alternative loans that are potentially available. However, it is not meant to be an exhaustive range of potential alternative loan products to the borrower. Loan originators are encouraged to discuss any alternative loan products

with borrowers and provide them with their own versions of tradeoff tables showing the effects of the alternative loan terms on interest rates, monthly payments, loan amounts, and settlement costs.

7. Establishing Meaningful Standards for GFEs.

a. Tolerances

Proposed Rule. Under the March 2008 proposed rule, loan originators would have been prohibited from exceeding at settlement the amount listed as "our service charge" on the GFE, absent unforeseeable circumstances. The proposed rule also would have prohibited the amount listed as the charge or credit to the borrower for the interest rate chosen, if the interest rate was locked, absent unforeseeable circumstances, from being exceeded at settlement. In addition, the proposed rule would have prohibited Item A on the GFE, "Your Adjusted Origination Charges," from increasing at settlement once the interest rate was locked. The proposed rule also would have prohibited government and recording fees from increasing at settlement, absent unforeseeable circumstances.

Under the March 2008 proposed rule, the sum of all the other services subject to a tolerance (originator-required services where the originator selects the third party provider, originator-required services where the borrower selects from a list of third party providers identified by the originator, and optional owner's title insurance, if the borrower uses a provider identified by the originator) would have been prohibited from increasing at settlement by more than 10 percent of the sum for services presented on the GFE, absent unforeseeable circumstances. Thus, a specific charge would have been able to increase by more than 10 percent, so long as the sum of all the services subject to the 10 percent tolerance did not increase by more than 10 percent.

Comments

Supporters of Tolerances

Many commenters expressed various degrees of support for the concept of tolerances. A trade group, representing mortgage brokers as well as some large lenders, expressed support for the concept of tolerances, albeit with certain clarifications or modifications. However, the strongest support for tolerances came from federal banking regulators and groups representing consumer interests. These commenters agreed that unexpected increases in costs between those provided in the GFE and those actually charged at settlement are a significant problem for prospective borrowers, and that the tolerances proposed by HUD would be an effective way of preventing such surprises. These commenters made various suggestions for strengthening the tolerance provisions to provide additional protections for borrowers. Suggestions included calculating the tolerances item-by-item rather than by grouping certain items together and strengthening enforcement.

Opponents of Tolerances

Most lenders, trade groups representing lenders, and trade groups representing other settlement service providers were generally opposed to the proposed tolerance provisions. These commenters stated that tolerances and particularly the zero tolerance for loan originator charges are equivalent to a settlement cost guarantee, and therefore conflict with the explicit statutory requirement for an *estimate* of settlement charges. Several commenters reviewed the legislative history of section 5 of RESPA, emphasizing that the statute was designed "to provide the prospective homebuyer with *general* information as to what their costs will be at the time of settlement." (See H.R. Rep. No.

667, 94th Cong., 1st Sess., at 2, 1975 U.S.C.C.A.N. 2448, 2449 (Nov. 14, 1975) (emphasis added).) These commenters also stated that tolerances may be inconsistent with the statutory provision permitting disclosure of a range of charges for settlement services.

Trade groups representing other settlement servicer providers, especially realtors and title companies, focused on the alleged potential anticompetitive effects of the tolerance provisions. These groups suggested that large lenders would seek to manage the risks associated with tolerances by contracting with large third party settlement service providers, thereby placing small settlement service providers at a competitive disadvantage.

Lenders and trade groups representing lenders and some other settlement service providers also strongly supported removing government recording and transfer charges from the tolerances. They stated that these charges are outside of the control of the loan originator and cannot be known with any certainty at the time the GFE is provided.

Several lenders and trade groups representing lenders suggested alternatives to the proposed tolerance provisions. For example, certain trade groups representing lenders recommended that tolerances not apply to the initial GFE, which would be used as a shopping tool, but tolerances would apply only to a "final" GFE that would be provided after a full mortgage application had been completed. These trade groups also supported more flexibility in the tolerance for the loan originator's own charges, and suggested a 5 percent tolerance rather than a "zero tolerance." Another alternative suggested by at least one lender was to evaluate overall compliance with tolerances rather than compliance on a loan-by-loan basis. This suggestion, according to the commenter, would alleviate many

of the difficulties in anticipating unusual aspects of individual loans but still hold lenders accountable for providing GFEs that, as a rule, accurately reflect charges at settlement. Another suggestion offered was to make providing a list of third party settlement service providers to prospective borrowers optional, with tolerances applying only where the loan originator selected the service provider or where the loan originator provided a list of service providers.

HUD Determination

Based on the comments received in response to the proposed rule, HUD has revised a number of provisions dealing with the tolerances. In particular, HUD has clarified the situations where the loan originator would no longer be bound by the tolerances. However, HUD has determined that only limited changes are necessary in the tolerance amounts for settlement service categories in the rule. The final rule seeks to balance the borrower's interest in receiving an accurate GFE early in the application process to enable the borrower to shop effectively, with the lender's interest in maintaining flexibility to address the many issues that can arise in a complex process such as loan origination.

Many commenters recommended changes to the size of the tolerances for different categories of settlement costs, especially the zero tolerance for loan originator charges. With one exception described below, the final rule does not change the amounts of the tolerances permitted for the different categories of settlement costs. As noted in the proposed rule, HUD considered the best available data on the variation in the costs of settlement services, in particular, for title services, in determining that a 10 percent

tolerance is reasonable. No commenters submitted or identified any alternative data sources that would support expanding the tolerances beyond 10 percent.

With respect to the zero tolerance for a loan originator's own charges, HUD recognizes the comments characterizing the tolerance as a potential settlement cost guarantee. However, the final rule provides substantial flexibility to loan originators in providing a revised GFE when circumstances necessitate changes. By providing such flexibility, HUD intends to prevent only those increases in the loan originator's charges that are made in "bad faith." Section 19(a) provides explicit authority for the Secretary to make such interpretations as may be necessary to achieve the purposes of RESPA. Providing a clear, objective standard for what constitutes "good faith" under section 5 of RESPA is necessary to provide more effective advance disclosure to homebuyers and sellers of settlement costs, and as such, falls directly within the Secretary's interpretive authority under section 19(a). In the context of residential mortgage negotiations, HUD finds that the term "good faith" requires that, once a loan provider has quoted in writing a certain price as the cost of its own services in a specific transaction and absent the "changed circumstances" provided for elsewhere in the rule, the provider must adhere to the quoted price.

The one exception to the amounts of the tolerances remaining the same as in the proposed rule is the tolerance for the government recording and transfer charges. HUD has adjusted how these charges are treated under the tolerances. The final rule splits the government recording and transfer charges into two categories: government recording charges, and transfer taxes.

Transfer taxes should generally be known at the time the GFE is provided, so those taxes continue to be subject to a zero tolerance. If there are changes in the tax rates or in the price of the property after a GFE is provided, those changes would either constitute changed circumstances or new information that would be the basis for providing a revised GFE. It is HUD's view that these provisions will provide sufficient flexibility to protect loan originators from changes outside their control, while still preventing loan originators from providing "low-ball" estimates of transfer taxes on the GFE that could mislead prospective borrowers. Government recording charges, in contrast, often may not be known with any certainty at the time the GFE is provided, and in many cases not until close to, or at, closing. Therefore, HUD has determined that these charges should be included with the third party charges that are subject to an overall 10 percent tolerance. Because the government recording charges typically are small in relation to other settlement costs, this should provide ample flexibility to loan originators on these charges without unduly impacting the permitted tolerances for other third party settlement charges.

As noted earlier in this preamble, HUD has made a number of changes to the tolerances provisions to clarify and provide additional flexibility in managing the tolerances. As in the proposed rule, the final rule adds a paragraph to the current regulations that provides that a loan originator that violates the GFE requirements, which include the tolerance requirements, shall be deemed to have violated section 5 of RESPA. However, the final rule also provides a loan originator with an opportunity to cure any violation of the tolerance by reimbursing the borrower any amount by which the tolerances were exceeded. This reimbursement may be made at settlement or within 30

calendar days after settlement. HUD will deem a payment to have been provided in a timely fashion if it is placed in the mail by the loan originator within 30 calendar days after settlement. HUD has determined, based on the comments received, that 30 calendar days provides sufficient time for loan originators to identify and cure any tolerance violations through their post-closing review process. In most cases, HUD expects that violations will be identified at or before settlement when completing the revised HUD-1 form, which provides a clear format for comparing the charges estimated on the GFE with those actually imposed at settlement.

The opportunity to cure violations of the tolerances is an important tool for loan originators to manage compliance with the tolerance requirements. Many lenders and groups representing lenders and other settlement service providers objected to the imposition of tolerances because of the difficulty of providing accurate estimates to prospective borrowers early in the application process. The opportunity to cure will permit loan originators to give an estimate of expected settlement charges in good faith, without subjecting them to harsh penalties if the estimate turns out to be lower than the actual charges at settlement.

HUD has also made clarifying changes to the proposed provision describing the circumstances in which the GFE can be revised. As described in more detail below, changed circumstances that result in higher costs can be a basis for providing a revised GFE. In addition, information that was either not known or not relied on at the time the original GFE was provided may also be the basis for providing a modified GFE.

b. Unforeseeable Circumstances.

Proposed Rule. The March 2008 proposed rule provided that loan originators would not be held to tolerances where actions by the borrower or circumstances concerning the borrower's particular transaction result in higher costs that could not have reasonably been foreseen at the time of the GFE application, or where other legitimate circumstances beyond the originator's control result in such higher costs. The proposed rule also provided that if unforeseeable circumstances would result in a change in the borrower's eligibility for the specific loan terms identified in the GFE, the borrower must be notified of the rejection for the loan and be provided a new GFE if another loan is made available.

Comments

Most of the commenters who commented on unforeseeable circumstances generally supported the proposed rule's provision on this matter, but many recommended changes or additions to the proposed definition of unforeseeable circumstances. Several lenders and trade groups representing lenders indicated that, while "unforeseeable circumstances" encompasses many things that would fall under the statutory requirement that estimates of settlement costs be in "good faith," the two concepts are not always equivalent. Some commenters suggested that the definition be expanded or clarified to include any situation that is outside the lender's control, even if such a situation involves a change that occurs often enough to be "foreseeable" in some sense. An example offered of such situation is one in which the changes in the price of the property or in the estimated value of the collateral may necessitate new information about the credit quality of the borrower that is developed during the underwriting process, or any other situation for which there is a reasonable explanation and that is still consistent with "good faith."

Several commenters, including FTC staff and a trade group representing mortgage brokers, found the proposed definition of "unforeseeable circumstances" to be vague. They suggested adding specific examples of common situations to clarify the scope of "unforeseeable circumstances."

These commenters also offered suggestions regarding the definition. A group representing consumer interests recommended that HUD carefully monitor how often unforeseeable circumstances override the tolerance requirements, to ensure that the exception does not swallow the rule. A joint comment letter from groups representing state regulators suggested that a provision be included requiring loan originators to provide written notice to borrowers describing the "unforeseeable circumstance" that resulted in the higher costs.

HUD Determination

Based on the comments received in response to the proposed rule, HUD has made a number of changes to the proposed provisions describing the circumstances in which the GFE can be revised. HUD has determined that changes are needed to the proposed grounds for providing a revised GFE.

The final rule clarifies the different types of circumstances ("changed circumstances") that can be a basis for providing a revised GFE. The final rule continues to emphasize that market price fluctuations by themselves are not changed circumstances. For example, if an appraiser that a loan originator intends to use for a particular transaction raises its prices by $50 after the loan originator has already provided a GFE, that increase would not have constituted an unforeseeable circumstance under the proposed rule. This result would continue under the final rule, i.e., such a price increase

by the appraiser would not be a "changed circumstance" allowing the issuance of a new GFE.

HUD recognizes that numerous commenters recommended elaborations of, or technical changes to, the definition of unforeseeable circumstances. Because many of the changes described in the proposed definition of "unforeseeable circumstances" happen frequently enough that they could be "reasonably foreseen," the final rule replaces the definition of "unforeseeable circumstances" with a new definition for "changed circumstances." However, the types of circumstances included in the new definition are similar to the types of circumstances that were included in the proposed rule. The first clause in the new definition of "changed circumstances" in the final rule still includes acts of God, war, disaster, or other emergencies as was included in the proposed rule. The final rule clarifies that the other circumstances in the second clause are separate from and in addition to the circumstances listed in the first clause. The final rule also clarifies that the other circumstances include situations where information particular to the borrower or the transaction either changes or is later found to be different from what was known at the time the GFE was provided. For example, new information affecting the borrower's credit quality or a change in the loan amount might occur often enough to be "reasonably foreseeable", but it would still fall within the types of circumstances included in the second clause of the definition of "changed circumstances."

Under the final rule, changed circumstances that result in an increase in settlement costs, such that the tolerances would be exceeded, or that result in a change in a borrower's eligibility for the loan offered, may be the basis for providing a revised GFE. For example, if the actual loan amount turns out to be higher than the loan amount

indicated by the borrower at the time the GFE was provided, and certain settlement charges that are based on the loan amount increase as a result, the loan originator may provide a revised GFE reflecting those higher amounts. Compliance with the tolerance provisions would be evaluated by comparing the revised GFE with the actual amounts charged at settlement.

Similarly, if underwriting and verification show that a borrower's monthly income is different from the income relied on in providing the original GFE, and the difference results in a change in the borrower's eligibility for that loan with those particular terms, the loan originator would no longer be bound by the original GFE. If a loan with different terms is available for that borrower, then the loan originator would have the option of providing a modified GFE. Conversely, as an example, if the borrower's total assets were relied on in providing the original GFE, and those assets are not materially different from what was stated at application, then the borrower's total assets may not be used as a basis for providing a revised or modified GFE.

While these changes are intended to provide loan originators with more flexibility in providing revised GFEs, HUD is also mindful of the potential for abuse. Unscrupulous loan originators might seek to avoid providing a reliable GFE by claiming not to have relied on information provided by the prospective borrower. In order to discourage loan originators from providing "generic" GFEs that are not based on a preliminary evaluation of a particular borrower, the final rule limits the ability of loan originators to provide a revised GFE based on information that was collected from the borrower prior to providing the GFE. However, if a loan originator documents that it relies on a limited range of information in providing GFEs to borrowers, the loan originator may provide a

revised GFE based on any other information that results in increased settlement costs or a change in the borrower's eligibility, even if the information was received by the loan originator prior to providing the GFE, subject to the provisions of the rule. Loan originators are presumed to have relied on the same minimum information that must be collected by the loan originator before providing a GFE; namely, the borrower's name, the borrower's monthly income, the property address, an estimate of the value of the property, the amount of the mortgage loan sought, and any credit report that is obtained by the loan originator before providing the GFE. These limitations on providing a revised GFE apply only if subsequent underwriting and verification confirm that the information remains substantially the same as the information provided by the borrower at the time of the GFE. For example, if the borrower's monthly income turns out to be substantially less than the monthly income stated by the borrower in the initial application, the final rule would not prevent the loan originator from either providing a revised GFE or from denying the loan altogether. If the loan originator decides to provide a revised GFE, HUD encourages the loan originator to explain to the borrower the reasons for providing a revised GFE based on the changed circumstances.

Several other provisions in the final rule that permit revisions to the GFE have not changed significantly from those proposed. The final rule provides that a revised GFE may be provided if a borrower requests changes in the loan product, such as changing from a 30-year term to a 15-year term, or from a fixed-rate mortgage to an adjustable rate mortgage. A revised GFE would be permitted whether such change is first suggested by the loan originator, or by any other party. The final rule also provides that if a prospective borrower does not express an intent to continue with an application within 10

business days of receiving the original GFE, or such longer time specified by the loan originator on the GFE, the loan originator is no longer bound by the GFE. While HUD does not intend for the GFE form to in any way affect state laws regarding contract formation, this provision is intended to make clear that the estimated charges on a GFE are not open-ended.

The final rule also clarifies that, where a borrower has not locked a particular interest rate, or where an interest rate lock has expired, all interest rate-dependent charges on the GFE are subject to change. The charges that may change include the charge or credit for the interest rate chosen, the adjusted origination charges, and per diem interest. The loan originator's origination charge, shown in Block 1 on page 2 of the GFE, is not subject to change, even if the interest rate floats. Of course, the various specific places where the interest rate is identified on the GFE would also be subject to change if the interest rate is not locked. If the borrower later locks the interest rate, a revised GFE should be provided at that time to show the revised information.

Finally, the final rule includes the proposed provision on revision of the GFE for transactions involving new home purchases. HUD recognizes that in cases of new construction, the original GFE may be provided long before settlement is anticipated to occur. In those cases, the loan originator may provide a clear and conspicuous disclosure to the borrower that a revised GFE may be provided at any time up until 60 calendar days prior to closing. If no such disclosure is provided, or if no revised GFE is actually given, then compliance with the tolerances will be evaluated by comparing the charges on the original GFE with the actual charges at settlement. During the 60 calendar days prior to

closing, a revised GFE may be provided only in accordance with the other paragraphs in this section.

In any case where a revised or modified GFE is provided to a prospective borrower, the loan originator is required to document the reasons for changes that are made and to maintain that documentation for 3 years after settlement.

8. Lender Disclosure

Proposed Rule. The proposed GFE included information for the borrower to note that lenders can receive additional fees from other sources by selling the loan at some point after settlement. However, the borrower was also informed that once the loan is obtained at settlement, the loan terms, the borrower's adjusted origination charges, and total settlement charges cannot change. The language on the proposed GFE also indicated that after settlement, any fees lenders receive in the future cannot change the loan received or the charges paid at settlement by the borrower.

Comments

Lender Representatives

Lenders and lender organizations commented that the disclosure regarding lender compensation on page 4 of the GFE is misleading and unnecessary, and should therefore be removed. These commenters suggested that because borrowers already understand how lenders are compensated, through origination charges and interest, lenders are already required to make full compensation disclosures. Sale of the loan after settlement merely allows the lender to collect the present value of that interest. One lender argued that secondary market sale of the loan actually reduces costs to borrowers rather than increases them. Lenders also commented that the disclosure is biased against lenders

because it does not point out that they can lose money selling the loan later. In addition, one lender said that the current servicing disclosure already covers this information. Lenders also suggested that because the text of the disclosure does not concern settlement costs or issues, the disclosure is outside the purview of RESPA.

Mortgage Broker Representatives

NAMB supported HUD's inclusion of the lender disclosure information, but felt that such information should be presented with greater emphasis and in more detail. NAMB suggested moving the information to page two of the GFE and presenting it as part of the YSP disclosure, in order to make clear to consumers the similarity in the two charges. According to NAMB, this change would help achieve parity of disclosures between lenders and mortgage brokers, which is essential for effective consumer disclosure.

Other Commenters

FTC staff commented that the lender disclosure is misleading and will cause confusion because it does not make clear that the terms of the loan may be dependent on anticipation of the secondary market fees described. FTC staff said there should be more explicit disclosure in the origination charge section of the GFE, making clear that lenders also get higher fees for a higher interest rate.

HUD Determination

After consideration of the comments, HUD has determined to retain the lender disclosure on the GFE. HUD is retaining the lender disclosure on the GFE because HUD believes that it is important for borrowers to be aware that lenders may receive additional fees by selling the loan after settlement. However, the disclosure has been streamlined.

The disclosure on the revised form informs the borrower that some lenders may sell the loan after settlement and any fees received by the lender for selling the loan cannot change the borrower's loan or the charges paid by the borrower at settlement.

9. Enforcement and Cure

Proposed Rule. The March 2008 proposed rule provided that HUD would deem violations of the requirements for the GFE in 24 CFR 3500.7 to be violations of section 5 of RESPA. This would include instances where the charges listed on the GFE are exceeded at settlement by more than the tolerances permitted under § 3500.7(e). In similar fashion, the proposed rule provided that HUD would deem violations of the requirements for the HUD-1/1A in § 3500.8 to be violations of section 4 of RESPA.

HUD invited comments on whether a provision should be added to the RESPA regulations that allow a loan originator, for a limited time after closing, to address the failure to comply with tolerances under the proposed GFE requirements, and if so, how such a provision should be structured. HUD sought comments on whether such a provision would be useful and, if so, what the appropriate time frame would be for finding and refunding excess charges. HUD also invited comments on whether the potential for abuse of such a provision would be harmful to consumers. Comments were also sought on whether the ability of prosecutors to exercise enforcement discretion would obviate the need for such a provision.

Comments

Many comments were received on the advisability of allowing loan originators to cure potential violations of the tolerances on the GFE. Lenders and trade groups representing lenders and some settlement service providers strongly supported the

addition of a provision allowing loan originators to cure potential violations of the tolerances. Several lenders reiterated their previous comment that HUD lacks authority to impose tolerance requirements on the GFE, but that if a tolerance provision were authorized by statute, they would support the inclusion of a cure provision. Among the lenders and lender trade groups that supported inclusion of a cure provision, the comments were almost evenly divided between those suggesting a 60-calendar-day period to cure potential violations of the tolerances, and those suggesting a 90-calendar-day period. Another commenter recommended that HUD consider adding a cure provision for the HUD-1 and closing script.

Consumer groups were generally supportive of stronger enforcement of RESPA's disclosure requirements, including enactment of statutory changes that would include civil money penalties for violations of those requirements. A consumer group that responded to HUD's question regarding a cure provision expressed its opposition to adding such a provision. Consumer groups, generally, raised the possibility that a cure provision could be abused by offering only partial reimbursement to a borrower. These commenters suggested that loan originators would have an incentive to cure violations even without a specific provision exempting them from liability if a potential violation is cured.

HUD Determination

Based on the comments received in response to the proposed rule and further consideration of this issue by HUD, HUD has determined that a cure provision is important to allow loan originators to more effectively manage any uncertainty in costs associated with the required tolerances on the GFE. By including a cure provision, HUD

recognizes that some errors are inevitable when handling large numbers of complex transactions, and HUD does not intend for the tolerance requirements to create liability for inadvertent errors.

As described in more detail above, HUD has built an opportunity to cure violations of the tolerances into the requirements establishing the tolerances. The final rule also provides that a violation of any of the requirements for completing the HUD-1/1A shall be deemed to be a violation of section 4 of RESPA. However, the rule provides that an inadvertent or technical error in completing the HUD-1/1A shall not be deemed a violation of section 4 of RESPA, if a revised HUD-1/1A is provided to the borrower and/or seller within 30 calendar days of settlement. This opportunity to cure errors on the HUD-1/1A is consistent with HUD's longstanding policy permitting settlement agents to provide revised HUD-1/1A settlement statements where errors are discovered after settlement.

10. Implementation Period.

Proposed Rule. In the March 2008 proposed rule, HUD stated that it intended to include a 12-month transition period in the final rule. During the 12-month transition period, settlement service providers and other persons could comply with either the current RESPA requirements or with the revised requirements of the amended provisions. HUD invited comments on whether such a transition period is appropriate.

Comments

Consumer representatives generally favored a 12-month implementation period, while lenders and their trade associations sought a longer implementation period on the basis that 12 months is insufficient time to prepare for compliance with the new

requirements. According to one major lender, a 12-month period is far too short, given the extensive nature of the changes. This lender estimated that an 18-24 month period will be required for implementation of the proposal, as published on March 14, 2008. According to other major lenders, the proposed rule would require significant systems and operational changes well beyond the complex forms changes, and would take a minimum of 2 years to implement. A lender association stated that requiring the industry to implement changes to RESPA disclosures and then to later implement changes to TILA disclosures would result in significant and duplicative costs for systems changes, training, and staffing that would ultimately be borne by consumers. This association expressed support for an implementation period beginning 18 months after the effective date of the rule, or 18 months after the implementation period for the Federal Reserve Board's TILA rule, whichever is later.

HUD Determination

HUD has determined to proceed with adoption of a 12-month implementation period. HUD recognizes that operational changes will be required in order to implement the new rule, in addition to training staff on the new requirements. However, the need for a standardized GFE with relevant information about the loan and settlement charges is critical in light of the problems in the current market, and further delay is not warranted. HUD believes that a 12-month implementation period will provide sufficient time for systems changes and training to occur. Therefore, use of the new GFE and the new HUD-1/1A will be required as of January 1, 2010. During the transition period, the current RESPA requirements with respect to the GFE and the HUD-1/1A remain in effect and settlement service providers may choose to proceed under either the current GFE and

HUD-1/1A requirements or may choose to proceed under the new GFE and HUD-1/1A requirements. However, any settlement service provider who delivers the new GFE prior to January 1, 2010, will be subject to all of the requirements related to the new GFE, including compliance with the tolerance provisions and use of the required HUD-1/1A.

Other provisions of this final rule, including the average charge and required use provisions and the technical amendments, are implemented immediately upon the effective date of the rule.

As previously stated, HUD will issue guidance on compliance with the rule's provisions during the implementation period.

C. Lender Payments to Mortgage Brokers – Yield Spread Premiums (YSPs)

1. Disclosure of YSP on GFE.

The March 2008 proposed rule provided that lender payments to mortgage brokers in table-funded and intermediary transactions be clearly disclosed to consumers on the GFE and the HUD-1 settlement statements, as set forth below. The rule also proposed to streamline the current regulatory definition of "mortgage broker."

Under the March 2008 proposed rule, the first page of the GFE presented the net origination charge as "your adjusted origination charges." The second page of the proposed GFE informed the consumer how the adjusted origination charge was computed. Block 1 disclosed as "Our service charge" the originator's total charge to the borrower for the loan. The rule proposed that in the case of loans originated by mortgage brokers, the amount in Block 1 would have to include all charges received by the broker and any other originator for, or as a result of, the mortgage loan origination, including any payments from the lender to the broker for the origination. In the case of loans

originated by originators other than mortgage brokers, the amount in Block 1 would have to include all charges to be paid by the borrower that are to be received by the originator for, or as a result of, the loan origination to the borrower, except any amounts denominated by the lender as discount points and which would be disclosed in Block 2.

In loans originated by mortgage brokers, Block 2 of the second page of the proposed GFE would have disclosed whether there is any charge or credit to the borrower for the specific interest rate chosen for the GFE. The second check box would have indicated whether there was a payment for a higher interest rate loan, described as the "credit of $ ____ for this interest rate of ___%. This credit reduces your upfront charges." The third check box would have indicated a "charge of $ for the interest rate of %. This payment (discount points) increases your upfront charges." Any lender payment would have been subtracted and any points would have been added to arrive at "your adjusted origination charge" that would also have been disclosed on the first page of the form. The proposed rule provided that for mortgage brokers, the amounts of any charge or credit in Block 2 would have to equal the difference between the price the wholesale lender pays the broker for the loan and the initial loan amount.

Comments

Consumer Representatives

Some consumer groups opposed the proposed YSP disclosure on several grounds. These groups asserted that to describe lender-paid broker compensation as a credit to reduce settlement costs is misleading. NCLC stated that there is no requirement that the lender payment will actually be used in this manner. CRL stated that the proposed language presumes a trade off through a reduction in upfront costs, and research shows

that this does not occur, except in limited circumstances. According to CRL, the disclosure's characterization of the YSP as a "credit" only exacerbates the issue of the nonexistent trade off. CRL expressed concern that the disclosure suggests that the arrangement is saving the consumer money, when in fact the disclosure is doing the opposite. CRL also objected to the disclosure on the grounds that the disclosure does not make clear that this is a fee paid to a broker. In addition, CRL stated that it found the disclosure confusing, and noted that HUD has not tested the effectiveness of the disclosure outside of controlled circumstances. Both CRL and NCLC recommended an alternative formulation for disclosure of mortgage broker compensation.

NCLC also stated that the proposed disclosure potentially complicates TILA review. According to NCLC, without guidance from the Federal Reserve Board, it is not clear what effect treating the lender-paid broker compensation as a credit will have on the central TILA disclosures, which are the finance charge and the APR.

Industry Representatives

Lenders generally were opposed to the proposed YSP disclosure. Many lenders and their trade associations asserted that the proposed approach for disclosing YSP conflicts with pending TILA and HOEPA rule changes proposed by the Federal Reserve Board, and is also inconsistent with Advisory Letter 2003-3 of the Office of the Comptroller of the Currency (OCC). These lenders stated that it would be costly and confusing for the banking industry if HUD and the Federal Reserve Board issued varying rules, revisions, and disclosures independently. Other lenders stated that, because in their view HUD assumed that the only way for a lender to calculate payment to the broker is by tying the compensation to the borrower's interest rate, neither the proposed GFE nor

the proposed HUD-1 can accommodate a lender's compensation payment to the broker based on the loan amount, or based on a flat dollar amount. According to these lenders, if a lender were to pay broker compensation that is not tied to the interest rate, there would be no way to disclose the payment without artificially inflating the charges paid by the borrower.

A major lender noted that if a broker intends to rely primarily on the lender for compensation, the dollar-for-dollar offset of the YSP against other service charges will necessitate that the broker increase the disclosed consumer paid fees. The lender commented that this has regulatory impacts under other laws. The lender stated that the origination fee is a finance charge under TILA. The lender also stated that the origination fee is also normally included in the points and fees definitions under several state high-cost laws and HOEPA, whereas YSP payments are only a finance charge under TILA to the extent included in the interest rate and are not always included in points and fees calculations. According to this commenter, the proposed definition will artificially force more loans into the "high cost" category which will further limit credit because many lenders do not originate these loans.

CMC stated that the proposed mortgage broker compensation disclosure wrongly conflates mortgage brokers and mortgage lenders. CMC noted that there are important differences between mortgage brokers and mortgage lenders in terms of roles in the transaction, compensation, and risk posed to consumers. CMC stated that the mortgage broker disclosure proposal fails to adequately address these differences. CMC expressed opposition to consolidating the charges of the lender and the broker together in a single "service charge" because, according to CMC, such consolidation effectively hides the

amount of the broker's total compensation from the borrower. CMC believes that borrowers should have this information and that failure or omission to disclose could cause harm. CMC stated that disclosing YSP as a credit and lumping the YSP together with (or offsetting it against) lender fees or discounts hides the YSP in a way that is confusing and potentially harmful to the borrower. CMC recommended that broker compensation be disclosed as shown in the RESPA/TILA forms and "mortgage broker fee agreement and disclosure" submitted with their comments.

MBA asserted that the proposed disclosure will be unclear to borrowers while the costs occasioned by the adoption of new terminology for mortgage broker fees will, in its opinion, be enormous. MBA noted that, in its opinion, the proposed disclosure does not allow for the possibility that, in the future, some brokers will be paid on a basis other than the loan's interest rate. In addition, MBA stated that as lenders and brokers perform distinct functions in the marketplace and are perceived differently by consumers, applying the same rules to them is ill-advised. MBA proposed an alternative mortgage broker compensation disclosure that discloses the total compensation for the broker's services and the amounts paid by the lender to the broker on the borrower's behalf.

NAMB reasserted its opposition to carving out one component of the cost of a mortgage loan for the "putative purpose of clarification and simplification." NAMB asserted that the proposed YSP disclosure would achieve the opposite result and would detract from the consumer's ability to understand and comparison shop. NAMB recommended that direct competitors should be treated the same to facilitate shopping and promote consumer understanding. NAMB stated that if HUD continues to require disclosure of originator compensation, HUD must require all originators to disclose the

premium value created by interest on the loan, and that HUD must provide a method for making that calculation.

According to NAMB, the proposed disclosure makes distinctions among mortgage originators with no basis for doing so, and in disregard of market realities. NAMB stated that the proposal seeks to enhance regulatory distinctions among groups of originators, long after such labels have lost their meaning in the marketplace. NAMB also criticized the proposal because it would, in NAMB's opinion, isolate a single component of cost – compensation –rather than aggregate cost. According to NAMB, compensation is relevant only to the extent that compensation serves as a "rough proxy for the difference between the par, or wholesale, loan rate and the rate quoted to the consumer." In the case of mortgage brokers, that difference is called "yield spread premium" or YSP; in the case of lenders, that difference is called "service release premium" or SRP. NAMB asserted that in both cases, that differential may be readily determined prior to closing at the time the interest rate is locked and should be disclosed. NAMB also asserted that the lender's compensation after the loan is sold is irrelevant, since such compensation does not affect the price paid by the borrower. According to NAMB, what is relevant is the incremental cost to the consumer assessed at the time of closing that is attributable to the differential between the loan rate and the wholesale rate. NAMB asserted that that figure can be computed and disclosed prior to closing and recommended that HUD specify how that computation should be done, and require disclosure of the resulting figure, or in the alternative, not require such disclosure by any originators.

NAMB asserted that the methodology of HUD's testing is flawed in two respects. According to NAMB, the contractor failed to test consumer understanding of loan terms and of comparative shopping when YSP was not disclosed. Instead, according to NAMB, the contractor assumed the answer to the fundamental question of whether YSP disclosure aided consumers in comparative shopping. NAMB also stated that the testing focused only on how, not whether, to disclose YSP. NAMB stated that in doing so, the proposal ignored FTC's earlier finding that disclosing just broker compensation created confusion and led consumers to make decisions contrary to their best interests.

NAMB also asserted that HUD's testing was flawed because the testing was not conducted among actual borrowers dealing with actual loan originators. According to NAMB, the tests fail to assess the consequences of disparate disclosures in actual competitive markets. NAMB noted that, in 2004 and 2007, FTC conducted extensive studies on consumer mortgage disclosures, with a particular focus on mortgage broker compensation disclosures. NAMB further stated that the 2007 FTC study restated the conclusion of the earlier study, noting that disclosure of broker compensation "created a substantial consumer bias against broker loans, even when the broker loans cost the same or less than direct lender loans, because the disclosures would have been required of brokers, but not direct lenders." (See 2007 FTC Study at 6, n. 14). NAMB also objected to the proposed mortgage broker compensation disclosure on the grounds that the proposed rule fails to evaluate how the proposed broker disclosure would relate to any of the currently mandated disclosures. According to NAMB, all 50 states regulate brokers and their compensation in various respects. Industry practice and lender requirements mandate further disclosures. NAMB asserted that to limit complexity and information

overload, HUD should consider how all current mortgage broker disclosures would relate to its proposal.

NAMB also commented that HUD has not adequately addressed how its proposed mortgage broker compensation disclosure relates to the Federal Reserve Board's proposed amendments to Regulation Z, or how HUD's proposal relates to the risk-based pricing regulations recently proposed by the Federal Reserve Board and FTC pursuant to the Fair and Accurate Credit Transactions Act of 2003 (73 FR 28 966 (May 19, 2008)). NAMB recommended that HUD seek public comment on the interaction between HUD's proposal, the proposed amendments to Regulation Z, and the pending risk-based pricing regulations before proceeding to finalize the March 2008 proposed rule.

Other Commenters

The National Association of Realtors (NAR) stated that it is unclear whether consumers will understand the proposed disclosure of discount points and YSPs. According to NAR, calling the YSP a "credit" to the borrower without explaining or making it clear that the YSP is tied to the interest rate may mislead or confuse a consumer.

The Conference of State Bank Supervisors, the American Association of Residential Mortgage Regulators, and the National Association of Consumer Credit Administrators commented that the proposed disclosure of YSP is not parallel with the Federal Reserve Board's proposed rule amending Regulation Z. These commenters urged HUD to work closely with the Federal Reserve Board to develop seamless regulations before finalizing the proposed rule.

Federal Agencies

FTC staff expressed support for the goal of improving consumer understanding of the costs and terms of mortgage loans. However, based on the results of past FTC and HUD mortgage disclosure research, FTC staff urged HUD to consider reevaluating its proposed broker compensation disclosures, because they may adversely affect consumers and competition. FTC staff stated that alternative disclosures that clarify the role of mortgage originators, applied equally to all originators, could provide greater benefits to consumers and avoid adverse effects on consumers and competition. FTC staff urged HUD to evaluate and test alternative disclosures to determine the type or types of disclosures that will most benefit consumers. FTC staff also suggested that HUD consider, and possibly test, whether other disclosures such as one that clarifies the role of all mortgage originators would be more beneficial for consumers.

The FDIC expressed some concerns about the proposal's approach to YSP disclosure. The FDIC stated that the proposed GFE does not clarify that YSP is a payment made by a lender to a mortgage broker in exchange for referring a borrower willing to pay an above par interest rate, nor does the GFE state the amount of the YSP to be paid to a broker. Instead, according to the FDIC, the GFE seems to presume that the lender will apply the YSP as a "credit" that will lower settlement costs by a corresponding amount. The FDIC noted that the proposal does not impose the condition that YSP must actually function as a credit to a borrower as a requirement on lenders or brokers. The FDIC further stated that while HUD's effort, through the March 2008 proposed rule, to provide borrowers with more information about the trade off between interest rates and settlement costs is positive, this information alone does not provide

borrowers with an understanding of the economic incentives motivating the lenders and brokers with whom the borrowers are dealing.

The FDIC recommended that HUD ban YSPs to ensure that broker compensation will not be based on steering the consumer to a loan that is more expensive than one for which the borrower otherwise would qualify. The FDIC recommended that HUD ban any mortgage broker compensation that is not a flat or point-based fee.

If YSPs continue to be permitted, the FDIC recommended that their purpose and cost be clearly disclosed. The FDIC recommended that the disclosure inform the consumer that the broker is receiving a payment from the lender for placing the consumer in a loan with a higher interest rate. The FDIC stated that a YSP should not be identified as a "credit," because such language would tend to make consumers believe that they are deriving a financial benefit from a YSP. The FDIC further recommended removal of the statement "(T)his credit reduces your upfront charge," because this language is not balanced by a corresponding statement that informs consumers that the YSP will result in them paying a substantially higher interest rate over the life of the loan.

HUD Determination

Having reviewed the comments, and based on its testing of the forms, HUD has determined to retain the mortgage broker disclosure as proposed, with clarifying modifications. However, in order to better explain how the disclosure works, HUD is removing, from § 3500.2 of the regulations, the definition of the term "charge or credit for the interest rate chosen" and at the same time inserting expanded information in the instructions on how to disclose the credit or charge to provide additional guidance.

In reaching the determination to retain the mortgage broker disclosure, HUD is mindful of the concerns expressed by the commenters, but believes that the mortgage broker disclosure, read in conjunction with the tradeoff table on the form, will help the borrower understand the relationship between the interest rate and the settlement charges. While many commenters claimed that the mortgage broker disclosure as proposed was confusing and would result in bias against mortgage brokers, HUD's testing of the form demonstrated that consumers understood the relationship between the interest rate and settlement charges as presented on the form and that no bias against brokers resulted from such disclosure. As noted below, while the substance of the broker disclosure remains the same in the final rule as it was in the proposed rule, some minor stylistic changes have been made to draw the borrower's attention to specific terminology in the disclosure that HUD believes will improve the disclosure.

Since 1992**,** HUD has required the disclosure of YSPs on the GFE and HUD-1 settlement statements as a "payment outside closing" or "POC." This means of disclosure has proved to be of little use to consumers. Moreover, notwithstanding that lender payments to brokers are directly based on the rate of the borrower's loan, under current HUD guidance such lender payments are not required to be included in the calculation of the broker's total charges for the transaction, nor are they clearly listed as an expense to the borrower. This omission is exacerbated by the fact that many brokers hold themselves out as shopping among various funding sources for the best loan for the borrower, while failing to explain to the borrower that the payment they receive from the lender is derived from the borrower's interest rate. While some brokers tell customers

how they can use lender payments to lower the customer's upfront settlement costs, others do not.

Policy Statement 2001-1 made clear that earlier disclosure and the entry of YSPs as credits to borrowers would "offer greater assurance that lender payments to mortgage brokers serve borrowers' best interests."(See 66 FR 53056.) HUD could not mandate new disclosure requirements in the Policy Statement. HUD did, however, commit itself in that Policy Statement to making full use of its regulatory authority to establish clearer requirements for disclosure of mortgage broker fees, and to improve the settlement process for lenders, mortgage brokers, and consumers. (See 66 FR 53053).

It is for this reason that HUD proposed its new disclosure requirements. HUD maintains that while rate-based payments to mortgage brokers must be clearly disclosed to borrowers, at the same time, mortgage brokers also must not be disadvantaged in the marketplace, since such disadvantage will only result in decreased competition and higher costs to consumers. Many mortgage brokers offer products that are competitive with and frequently lower priced than the products of retail lenders, and HUD wishes to preserve continued competition and lower prices for consumers, as well as consumer choice.

The revised GFE form in today's rule is the result of an iterative testing process, comprised of six rounds of consumer testing of the form during the period 2003 through 2007. An additional round of testing was conducted in the summer of 2008. Working with HUD, HUD's testing contractor used the data collected during each round to improve and modify the form throughout the testing process. A summary report on each

round of testing is available at:

<http://www.huduser.org/publications/hsgfin/GoodFaith.html>.

HUD disagrees that its contractor's consumer testing of the GFE form was flawed. Independent reviews by experts in consumer testing and forms development found no flaws in the design of the tests. NAMB's suggestion of testing forms in actual transactions is not necessary or workable. Properly designed and implemented testing does produce correct results through an iterative process. The most difficult aspect of testing actual transactions would likely be finding loan originators (both brokers and lenders) willing to develop and test a form that is designed to improve consumer understanding in actual transactions and thereby reduce the originators' information advantage and market power in those transactions. Perhaps as difficult would be keeping tested consumers from shopping outside of the experimental group of originators to keep the test valid, especially since the forms so strongly urge consumers to shop among different originators.

The NAMB's second criticism is also not valid as the third round of testing was exactly on the point of whether to disclose the YSP. The purpose of the YSP disclosure is to inform consumers about the full cost of originating loans through a broker and to help them to understand the tradeoff between interest rates/monthly payments and origination costs so that consumers can use the relationship to their benefit. The third round of testing did not include the YSP disclosure, and the important finding was that, without the YSP disclosure, consumers did not understand the existence of the tradeoff between interest rates and origination charges as well as when the YSP was disclosed. Helping consumers understand this tradeoff is a fundamental goal of HUD's RESPA

reform effort and of the design of the GFE form. The third round of testing confirmed that inclusion of the YSP disclosure helped consumers understand the tradeoff, and that if they take a loan with a relatively high interest rate, they should pay lower settlement charges. Since the need for the YSP disclosure to improve consumer understanding of the tradeoff was established in round 3, whether a YSP disclosure should be included was not the subject of later rounds of testing. Rather, later rounds of form development and testing were aimed at making the YSP disclosure free of anti-broker bias. This effort was successful. HUD's testing found that participants using HUD's GFE were successful more than 90 percent of the time in identifying the cheapest loan whether the GFE loan was from a lender, mortgage broker, or the two loans cost the same.

As indicated, HUD has maintained the disclosure on the top of page two of the revised GFE, while making some stylistic changes to this portion of the form in the interest of borrower comprehension. The top of page 2 refers to "Your Adjusted Origination Charges" instead of "Your Loan Details" on the proposed form because this is the section of the disclosure that sets forth the origination charges. The box on the top of page 2 informs the borrower how the adjusted origination charge is computed. In response to comments recommending that "service" charge be deleted from the form, Block 1 now discloses as "Our origination charge" the originators' total charge to the borrower for the loan.

The final rule requires that in the case of loans originated by mortgage brokers, the amount in Block 1 must include all charges to be paid by the borrower that are to be received by the broker and any other originator for, or as a result of, the mortgage loan origination, including any payments from the lender to the broker for the origination. In

the case of loans originated by originators other than mortgage brokers, the amount in Block 1 must include all charges to be paid by the borrower that are to be received by the originator for, or as a result of, the loan origination to the borrower, except any amounts denominated by the lender as discount points, which are disclosed in Block 2.

Block 2 discloses for loans originated by mortgage brokers whether there is any charge or a credit to the borrower for the specific interest rate chosen for its GFE. The heading for Block 2 of the proposed form included the term "points" at the end of the sentence. On the final form, this sentence now states, "Your credit or charge (points) for the specific interest rate chosen." The second check box indicates whether there is a payment for a higher interest rate loan described as the "credit of $_____for this interest rate of _____%. This credit *reduces* your settlement charges." The word "settlement" has replaced the word "upfront" from the proposed form to be more consistent with other terminology on the form. The third check box indicates any "charge of $_____ for this interest rate of _____%. This charge (points) *increases* your total settlement charges." Any lender payment is then subtracted and any points are added to arrive at "your adjusted origination charges". The final rule also requires that in the case where a lender compensates a broker based on a flat dollar amount, or based on the loan amount, the second box in Block 2 on page 2 must be checked.

At page 2, while lenders are not required to check the second or third boxes of Block 2, in loans where they do not make such disclosures, they are required to check Box 1 that indicates that "The credit or charge for the interest rate of _____% is included in 'Our origination charge.'" If lenders separately denominate any amounts due from the borrower as "points," they must check the third box indicating that there are charges for

the interest rate and enter the appropriate amount for points as a positive number. If lenders separately denominate any amounts as a credit to the borrower for the particular interest rate covered by the GFE, they must check the second box and enter the appropriate amount as a negative number. Lenders must also add any such positive amounts or deduct any negative amounts to arrive at "Your Adjusted Origination Charges," listed on Line A of page two of the form.

In reaching its determination, HUD considered providing only the adjusted origination charge without the calculation, and disclosing the YSP and points elsewhere on the form. HUD concluded, however, that a complete disclosure of the payments to the mortgage broker as presented on page 2 of the revised form, especially when read in conjunction with the tradeoff table on page 3, is valuable to borrower understanding of: (1) the broker's total compensation; (2) how rate-based payments from lenders can help reduce borrowers' upfront origination charges and settlement costs in brokered loans; and (3) how payments to reduce the interest rate and monthly charges increase upfront charges.

As discussed above, testing by HUD's contractor demonstrated that disclosure of the YSP out of context was not useful to consumers. On the other hand, a form that requires that lenders disclose that credits or charges may be included in their service charge as well, even when the calculation for brokered loans is on the form, was not confusing for borrowers. HUD's testing demonstrated that borrowers correctly compared adjusted origination charges between loans from mortgage brokers and loans from lenders even when the YSP is included in the calculation of the adjusted origination charge. Nevertheless, to assure that borrowers choose the best value loan without being

confused by the presence of a YSP, HUD established the first page of the GFE as a summary page that only includes total estimated settlement charges. HUD also considered the comments that its proposed mortgage broker disclosure requirement might be inconsistent with the approach taken by the Federal Reserve Board in its proposed rule to amend Regulation Z of TILA, 16 U.S.C. 1601, et seq. (73 FR 1672, January 9, 2008). However, the Federal Reserve Board recently announced that it has withdrawn its proposed mortgage broker fee agreement requirement set forth in its proposed rule (73 FR 44522, July 30, 2008).

In its consultations with the Federal Reserve Board staff, HUD raised the concerns expressed by some commenters that treating lender payments to mortgage brokers as a credit toward the origination charges could increase the points and fees of each brokered mortgage loan, thereby resulting in more loans coming under HOEPA coverage. Federal Reserve Board staff advised HUD that notwithstanding HUD's changed requirements, determinations of whether payments to a mortgage broker must be included in the finance charge and whether a loan is covered by HOEPA are based on the statutory definitions and requirements in TILA, as implemented by the Federal Reserve Board's Regulation Z, which are unaffected by HUD's RESPA rulemaking.

2. Definition of "Mortgage Broker."

The March 2008 proposed rule would have streamlined the current regulatory definition of "mortgage broker." Under the proposed definition, "mortgage broker" would mean a person (not an employee of the lender) or entity that renders origination services in a table-funded or intermediary transaction. The definition would also have applied to a loan correspondent approved under 24 CFR 202.8 for FHA programs. The

proposed definition would have eliminated the current exclusion of an "exclusive agent" of a lender from the current definition of "mortgage broker." Therefore, under the proposed rule, an "exclusive agent" of a lender who was not an employee of the lender, but who renders origination services in a table funded or intermediary transaction, would have been subject to the mortgage broker disclosure requirements set forth in the proposed rule.

Comments

Consumer groups did not comment on this issue. A lender association commented that the proposed change may be inconsistent with Regulation Z Comments 226.19-b-2(i) and 226.19(b)-3 concerning intermediary agents or brokers and the timing of disclosures. MBA stated that the definition should not be changed to include exclusive agents of lenders. MBA commented that because mortgage lenders, including their agents and employees, are functionally different from mortgage brokers, they should be treated differently. MBA stated that it does not believe that mortgage lenders or their exclusive agents warrant the same treatment as mortgage brokers. MBA asserted that borrowers do not perceive brokers in the same way as lenders and brokers do not present the same risks as lenders. MBA also stated that that term "intermediary" should not be injected into the definition at all, unless this term is clearly defined to cover independent mortgage brokers. According to MBA, because the term is undefined, "intermediary" could be misinterpreted to cover some loan officers who work for lenders and may be independent contractors.

NAMB expressed opposition to the proposed change because, according to NAMB, it would perpetuate distinctions among mortgage originators that no longer have

meaning in the marketplace. NAMB noted that the roles of mortgage brokers and other originators have converged with the ubiquity of the "originate to distribute" model of mortgage finance, and that the regulatory structure under RESPA should reflect that fact. NAMB recommended that, at a minimum, the definition of "mortgage broker" be expanded to include any originator that sells loans where servicing is released within 6 months of origination, rather than securitizing them or holding them in portfolio.

CSBS, AARMR, and NACCA supported the proposed change in the definition of mortgage broker, but recommended that HUD define "intermediary transaction." These commenters stated that by failing to define "intermediary transaction," HUD has created potential confusion among industry participants and regulators.

HUD Determination

HUD has determined to revise the definition of "mortgage broker." While HUD recognizes that mortgage lenders are functionally different from mortgage brokers, an exclusive agent of a lender who is not an employee of a lender, but who renders origination services and serves as an intermediary between the lender and the borrower, is essentially acting as a mortgage broker, and will be subject to the mortgage broker disclosure requirements, as set forth in the rule. This definition will also apply to a loan correspondent approved under 24 CFR 202.8 for Federal Housing Administration (FHA) programs.

The revised definition clarifies that a mortgage broker also means a person or entity that renders origination services and serves as an intermediary between a borrower and a lender in a transaction involving a federally related mortgage loan, including such a person or entity that closes the loan in its own name in a table-funded transaction.

3. FHA Limitation on Origination Fees of Mortgagees.

Under its codified regulations, HUD places specific limits on the amount a mortgagee may collect from a mortgagor to compensate the mortgagee for expenses incurred in originating and closing a FHA-insured mortgage loan (see 24 CFR 203.27). [1] The March 2008 proposed rule would have removed the current specific limitations on the amounts mortgagees are presently allowed to charge borrowers directly for originating and closing an FHA loan. Under HUD's proposal, the FHA Commissioner would have retained authority to set limits on the amount of any fees that mortgagees charge borrowers directly for obtaining an FHA loan. In addition, the proposed rule would have also permitted other government program charges to be disclosed on the blank lines in Section 800 of the HUD-1/1A.

Comments

There was little comment on this issue. NCRC disagreed with the proposal to remove the specific limitations on the amount mortgagees are allowed to charge for originating and closing an FHA loan. NCRC stated that a government-guaranteed loan product should shield borrowers from excessive charges by establishing reasonable limits on fees. According to NCRC, while it may be acceptable to carefully raise origination fee limits, this should be done only in conjunction with establishing reasonable limits on YSPs. This commenter stated that by establishing standard limits on origination fees and

[1] Under 24 CFR 203.27 (a)(2)(i), origination fees are limited to one percent of the mortgage amount. For new construction involving construction advances, that charge may be increased to a maximum of 2.5 percent of the original principal amount of the mortgage to compensate the mortgagee for necessary inspections and administrative costs connected with making construction advances. For mortgages on properties requiring repair or rehabilitation, mortgagor charges may be assessed at a maximum of 2.5 percent of the mortgage attributable to the repair or rehabilitation, plus one percent on the balance of the mortgage. (See 24 CFR 203.27(a)(2)(ii), and (iii).)

YSPs, the FHA loan product can keep the nongovernment guaranteed products competing by constraining direct fee and YSP costs.

HUD Determination

HUD believes that its RESPA policy statements on lender payments to mortgage brokers restrict the total origination charges for mortgages, including FHA mortgages, to reasonable compensation for goods, facilities, or services. (See Statement of Policy 1999-1, 64 FR 10080, March 1, 1999, and Statement of Policy 2001-1, 66 FR 53052, October 18, 2001.) Moreover, the improvements to the disclosure requirements for all loans sought to be achieved as a result of this rulemaking should make total loan charges more transparent and allow market forces to lower these charges for all borrowers, including FHA borrowers. Therefore, HUD has determined to finalize the proposed rule to remove the current specific limitations on the amounts mortgagees presently are allowed to charge borrowers directly for originating and closing an FHA loan. The FHA Commissioner retains authority to set limits on the amount of any fees that mortgagees charge borrowers directly for obtaining an FHA loan.

IV. Modification of the HUD-1/1A Settlement Statement.

A. Overall Comments on Proposed Changes to HUD-1/1A Settlement Statement

Proposed Rule. Under the March 2008 proposed rule, the current HUD-1/1A Settlement Statements would have been modified to allow the borrower to easily compare specific charges at closing with the estimated charges listed on the GFE. The proposed changes would have facilitated comparison of the two documents by inserting, on the relevant lines of the HUD-1/1A, a reference to the corresponding block on the GFE,

thereby replacing the existing line descriptions on the current HUD-1/1A. The proposed instructions for completing the HUD-1/1A would have clarified the extent to which charges for individual services must be itemized.

Comments

Consumer Representatives

A consumer group stated that while referencing the GFE lines on the settlement statement is an important step, HUD should mandate a summary settlement sheet that corresponds exactly to the summary sheet of the GFE. According to this group, doing so would obviate the need for a crosswalk between the GFE and the settlement statement. The consumer group stated that the HUD-1 should be easily comparable to the GFE and should facilitate, rather than hinder TILA and HOEPA compliance. The consumer group expressed concern that HUD's improvement of disclosures in the settlement context could impede review of lender compliance with the disclosure requirements under TILA. This commenter noted that the proposed HUD-1 would require lenders to disclose as a lump sum their origination charges and all title services. While this group stated that such an approach is an improvement from the perspective of consumer understanding, the group stated that not all origination and title services are clearly all in, or all out of, the TILA finance charge. Under TILA, for example, title insurance is excluded from the finance charge. The commenter stated that other charges related to title insurance, including the settlement fee, courier fee, or document preparation fees, may be included in the finance charge, particularly if they are not bona fide and reasonable. This commenter noted that similar inconsistencies are true of other origination fees. The commenter stated that absent coordination with the Federal Reserve Board on a more

useful and expansive definition of the finance charge, and statutory changes to TILA itself, the final settlement statement should not bundle either all title or all origination charges. The commenter also called for itemization of all title services on both the GFE and HUD-1, so that consumers are aware of the variety of fees.

Lender Representatives

Lenders commenting on the March 2008 proposed rule generally stated that the HUD-1 should be in the same format as the GFE, to enable comparisons of estimated and actual charges. A lender association stated that the proposed changes to the HUD-1 fall short of making the GFE and HUD-1 correspond. Many lenders expressed the concern that the way the proposed HUD-1 forms are to be completed would require many changes with significant operational and technology impacts. A major lender stated that changes to the HUD-1 that consolidate disclosures raise questions about the lenders' ability to complete post-closing checks of finance charge calculations.

Mortgage Broker Representatives

Mortgage brokers commented that the HUD-1 and GFE should mirror each other and promote clarity, understanding, and ease of use for consumers. However, because the proposed GFE, at four pages, is less user-friendly in their opinion than the current version, mirroring the HUD-1 after the proposed document will not make it easier for consumers to understand and use. In regard to specific items on the new HUD-1, one broker commented that specific lines such as the splitting of title insurance between lenders and owners would not work properly. In addition, the broker commented that the form of disclosure for closing services would interfere with "title only" agencies, and that the form of the HUD-1 would not leave room for an acknowledgment and certification.

Title and Closing Industry Representatives

Commenters from the title industry said that the HUD-1 was still not easily comparable to the GFE. They also suggested that the title insurance disclosure requirements would conflict with the laws of some states. One title insurance company recommended that title and closing charges be kept separate.

The title industry was opposed to the breakout of the title premium between the agent and the underwriter. It was suggested that this was a private business matter and that this breakout had no effect on the amount of the premium charged. Also, the breakout does not appear on the GFE, so it will not help the consumer to see it at closing.

One escrow company objected to HUD referring to tax and insurance deposits as "escrows" and said that the proper term was "impounds." Escrow companies also objected to HUD's reference to "optional" owner's title insurance and felt such reference might lead borrowers to forego needed protection. One suggested that the term "non-required" would be preferable, but pointed out that in some states owner's title insurance actually is required.

One escrow company commented that HUD tested only its own forms, not the forms submitted by others, so there was no evidence that HUD's forms were better. This commenter went on to say that it does not believe that consumers in a real-world situation will use these forms in the intended manner.

One closing attorney commented that the limiting of lender charges to line 801 will interfere with disclosure of such fees as an "underwriting fee," "desk underwriting fee," "table funding fee," and "MERS fee." This attorney also pointed to other

operational problems with the HUD-1 and suggested that the agent/underwriter split in the title insurance premium serves no useful purpose.

HUD Determination

HUD continues to agree with the many commenters who pointed out the importance of comparability between the GFE and the HUD-1. Accordingly, to facilitate comparison between the HUD-1 and the GFE, each designated line in Section L on the final HUD-1 includes a reference to the relevant line from the GFE. Borrowers will be able to easily compare the designated line on the HUD-1 with the appropriate category on the GFE. Terminology on the HUD-1 has been modified as necessary to conform to the terminology of the GFE. For example, since Block 2 on the GFE is designated as "your credit or charge (points) for the specific interest rate chosen", Line 802 on the HUD-1 is also designated "your credit or charge (points) for the specific interest rate chosen." Because Block 3 of the GFE "Required services that we select" will include multiple services such as appraisal, credit report, tax service and flood certification, each of these services are designated on separate lines of the HUD-1, with a notation that each is from GFE Block 3. The amount listed on the HUD-1 to be paid in advance for the mortgage insurance premium (included in the 900 series on the HUD-1) also contains a notation that the advance payment is from GFE Block 3. By noting the appropriate block from the GFE on each designated line of the HUD-1, borrowers will be able to easily compare the charges listed on the HUD-1 with the charges listed on the GFE.

With respect to the 1100 series for Title Insurance, the final HUD-1 includes designated lines for title services and lender's title insurance at line 1101, with a notation that this amount is from GFE Block 4. Unlike the proposed HUD-1, the final HUD-1

includes a designated line for the settlement or closing fee at line 1102, which is also from GFE Block 4. However, in order to limit unnecessary itemization of the component parts of the charge for title services, administrative and processing services related to title services must be included at line 1101 with the overall charge for title services. Because the final rule more clearly specifies the extent of itemization permitted, HUD has determined that it is no longer necessary to define "primary title services" as a particular set of title services. In addition, the final HUD-1 includes a designated line for owner's title insurance at line 1103, from GFE Block 5, but the reference to "optional" owner's title insurance was dropped from the proposed rule in response to comments. HUD has determined to retain the designated lines for the agent's portion of the total title insurance premium (Line 1107) and the underwriter's portion of the total title insurance premium (Line 1108). Although inclusion of the agent/underwriter split on the HUD-1 differs from the GFE, it is HUD's view that this breakdown will help consumers better understand their title charges.

To further facilitate comparability between the GFE and HUD-1, HUD has determined to include a third page to the HUD-1 that includes a chart comparing the amounts listed for particular settlement costs on the GFE with the total costs listed for those charges on the HUD-1. For further discussion of this chart, see the discussion of the Closing Script issue in the next section.

B. Proposed Addendum to the HUD-1, the Closing Script.

Proposed Rule. Under the March 2008 proposed rule, an addendum would have been added to the HUD-1/1A that would have compared the loan terms and settlement charges estimated on the GFE to the final charges on the HUD-1 and would have

described in detail the loan terms for the specific mortgage loan and related settlement information. The settlement agent would have been required to read the addendum aloud to the borrower at settlement and provide a copy of the addendum at settlement.

Comments

Consumer Representatives

NCLC, while supportive of the closing script, requested that HUD "clarify that lenders are responsible for the accurate delivery of the closing script" and "clarify that settlement agents also are responsible to the borrower for the accurate delivery of the closing script." NCRC supported the Department's inclusion of the closing script. It commented that the script would "instill integrity and prevent lenders from changing loan terms and costs between the application stage and loan closing." NCRC stated that the script would lead borrowers to have a "clearer understanding of loan terms and conditions."

The California Reinvestment Coalition also supported the inclusion of the closing script, but expressed concern that the script would not be useful to borrowers who are not fluent in English and to hearing-impaired borrowers. One consumer group expressed concern for circumstances when a borrower does not have an escrow account. In this event, the group expressed its hope that the closing script would provide an estimate of monthly payments for taxes and hazard insurance.

Industry Representatives

Title and Settlement Agents and Notaries

Most comments from title and settlement agents opposed the concept of the closing script and expressed the concern that any requirement to read a closing script to

the borrower and explain discrepancies between the GFE, the HUD-1 and the loan documents would constitute the "unauthorized practice of law." ALTA commented that in many states, settlement agents risk engaging in the unauthorized practice of law by reviewing loan documents and answering borrower questions about final loan terms. ALTA also stated that even in states where there are no concerns about the unauthorized practice of law, the proposed closing script requirements would add a significant additional amount of time to each closing, leading to a decrease in the number of closings a settlement agent can perform. According to ALTA, this will result in higher closing fees charged to the borrower and the seller. ALTA and others also raised concerns about how the closing script requirement would be implemented in those jurisdictions that do not conduct in-person closings. These commenters also questioned how the closing script requirement would be implemented if the borrower's primary language was other than English.

The National Notary Association and the American Society of Notaries (ASN) commented that notaries are not attorneys or actual settlement agents and do not have the authority to explain settlement terms to borrowers. The ASN also noted that "[b]y statute, notaries are strictly prohibited from explaining documents or giving any advice that can be seen as unlicensed practice of law." Other notaries and signing agents questioned what they would be required to do if GFE tolerances were exceeded or the borrowers asked questions they were unable to answer. They were particularly concerned that the requirement of reading, explaining, and noting any inconsistencies such as a GFE tolerance violation would cause them to be replaced by settlement agents and attorneys better able to address borrower's questions.

Many settlement agents also stated that they were unable to address borrower questions since they were not privy to discussions and decisions between the loan originator and borrower. ALTA suggested that the lender should bear the duty of preparing and delivering the closing script to the borrower.

Lenders

Lenders and their trade associations were generally opposed to the closing script requirement. Lenders commented that a mandatory closing script is unnecessary and will add new, substantive burdens to both lenders and settlement agents and ultimately increase closing costs. These commenters further asserted that the additional time involved in preparing the script and reading it at each closing will, over time, result in an increase in fees charged by lenders and settlement agents.

MBA stated that the script would "raise legal concerns, be too costly, provide little benefit to the consumer at closing and raise significant operational concerns." MBA also questioned HUD's authority to require an "additional disclosure."

Bank of America commented that it agreed with HUD's goal of reducing consumer confusion and dissatisfaction with the closing process, but asserted that the closing script will not resolve those issues. Bank of America stated that the disclosure of loan terms by use of a closing script would detract from the information that is disclosed in the TILA disclosure and could create more confusion than clarity. This commenter also asserted that the script does not take into account the realities of different closing practices in different parts of the country.

Peoples National Bank stated its belief that the script would add little to consumer's knowledge but would add significantly to the number and cost of documents

the lender must produce: "The fact that some predatory lenders have intentionally deceived consumers will not be cured by additional disclosures, whether on provided paper or read aloud." This commenter encouraged HUD to address issues related to deceptive practices through "more effective investigation and enforcement."

Mortgage Brokers

NAMB expressed its opposition to the closing script because it would "increase costs for consumers and lower the number of loans that can be closed in a day." Further, NAMB estimated that the additional time and resources that would be consumed by implementing the closing script would average approximately $500 per loan, with "no commensurate, or even discernible, benefit to consumers in light of disclosures already mandated." NAMB further questioned whether the script would bring mortgage brokers into an advisory role that might then trigger "state regulatory and licensing requirements" and liability.

Other Industry Representatives

The Real Estate Service Providers Council (RESPRO) opposed the closing script concept and raised the concern that reading the script aloud in the presence of third parties raises privacy issues under the Gramm-Leach-Bliley Act, which prohibits the dissemination of personal information.

HomeServices of America, Inc. (HomeServices) wrote that "the proposed closing script requirement is problematic and should not be implemented [because it] will not fulfill the purpose for which it is intended because it comes too late in the process and would be too costly." HomeServices asserted that the closing script would be ineffectual because "many buyers would be contractually obligated to conclude the real estate

transaction regardless of any inconsistencies between the GFE, the HUD-1 Settlement Statement and other loan documents and shown in the closing script."

Other Commenters

The National Association of Insurance Commissioners, while expressing general support for the closing script, expressed its belief that borrowers would be better protected "if the same information would be provided in writing earlier in the real estate transaction." The Office of the Illinois Attorney General supported the closing script and expressed the hope that by highlighting changes in terms and fees that have occurred since the GFE stage, "(t)he script will discourage loan originators from changing key loan terms and imposing additional charges at closing, practices commonly seen in investigations conducted by our office." This commenter further recommended that the HUD-1 Settlement Statement and closing script addendum "be *required* to be given to *all* borrowers 24 hours in advance, in addition to the requirement that the script be read aloud at closing."

CSBS, AARMR and NACCA, while supporting the closing script, expressed concern about the acknowledgement page, believing that the script may unintentionally release the settlement agent and/or loan originator from liability. CSBS stated "[p]erhaps of greatest concern to state supervisors, however, is if a consumer signs an acknowledgment stating they have been presented with the closing script and understand all portions therein, the lender will effectively be granted safe harbor if accused of deceptive tactics." They recommended that the acknowledgement be changed to indicate merely that the borrower was "presented with the closing script," in order to avoid granting the lender safe harbor.

Federal Agency Commenters

The FDIC commented that the closing script is helpful in making plain the negative financial consequences for a consumer of entering into an "unconventional loan product such as an interest-only loan." However, the FDIC stated that one shortcoming of the script is that there is no information about what a consumer can do if the loan originator exceeds the permissible tolerance.

The Office of Thrift Supervision (OTS) stated that while well intended, the proposed closing script requirement would be "time consuming and may neither be viable nor appropriate in all cases." OTS suggested that if the final rule contains a closing script requirement, a written script may suffice.

While expressing its general support of the script, the FTC staff suggested that HUD consider modifications to the current proposal. FTC staff recommended placing responsibility for creating the script on lenders, rather than settlement agents and stated that, at a minimum, lenders should have the responsibility of completing as much of the closing script as possible, to decrease the risk of inaccuracies. In addition, FTC staff recommended that HUD consider making the closing script and the comparison chart more consistent with the revised GFE and HUD-1 formats. FTC staff also recommended that the final rule address the responsibilities of settlement agents if there are inconsistencies between the loan terms and charges in the GFE and those in the HUD-1 and other loan documents and also recommended additional consumer testing of the script.

HUD Determination

In response to comments received on the proposed rule and HUD's further review, HUD has eliminated the closing script requirement. However, HUD continues to believe that borrowers should be apprised of their loan terms at the closing and should also be apprised of any differences between the amounts stated on the GFE and the amounts listed on the HUD-1 settlement statement. Accordingly, to ensure that borrowers are made aware of the final settlement charges and the terms of their loan, and to help make certain that borrowers get the settlement charges and loan terms to which they agreed, HUD is requiring an additional page on the HUD-1/1A settlement statement that sets forth a comparison between the charges listed on the GFE and the charges listed on the HUD-1/1A, and summarizes the final loan terms of the borrower's loan.

By eliminating the closing script, as proposed, and including information about the loan on the additional page of the HUD-1/1A Settlement Statement, borrowers will receive the essential information that was included in the proposed closing script while eliminating potential operational challenges posed by the proposed closing script.

The instructions for completing the HUD-1/1A settlement statement provide that the loan originator shall transmit sufficient information to the closing agent to allow the closing agent to prepare the HUD-1/1A, including the new last page. The first half of the new page includes a comparison chart that sets forth the settlement charges from the GFE and the settlement charges from the HUD-1/1A to allow the borrower to easily compare whether the settlement charges exceed the charges stated on the GFE. The second half of the new page sets forth the loan terms for the loan received at settlement in a format that reflects the summary of loan terms on the first page of the GFE, but with additional related information that would be available at closing. By presenting the comparison

chart and the loan terms on the new page of the HUD-1, the borrower will be made aware of any changes to the settlement charges or loan terms and be able to confirm those changes.

V. Permissibility of Average Cost Pricing and Negotiated Discounts – Discussion of Public Comments

A. Overview and Definition of "Thing of Value."

Proposed Rule. The March 2008 proposed rule would recognize pricing techniques that result in greater competition and lower costs to consumers, specifically average cost pricing and some discounts among settlement service providers, including volume based discounts. The rule proposed to amend 24 CFR 3500.8 and would have explained that charges for third party services may be calculated using average cost pricing mechanisms based on appropriate methods established by HUD. These mechanisms would also have accommodated volume based discounts. The proposed rule would have allowed loan originators to disclose on the HUD-1 an average cost price in accordance with one of several specific methods. The proposed rule also would have amended 24 CFR 3500.14(d) and the definition of "thing of value" to clarify that it would be permissible for settlement service providers to negotiate discounts in the prices for settlement services, so long as the borrower is not charged more than the discounted price.

Comments

Consumer Representatives

NCLC and CRL supported volume based discounts so long as the discounts were passed along to the consumer. However, CRL expressed concern that discounts may lead

originators to steer consumers to certain settlement service providers, thus limiting consumers' choice of servicers. Therefore CRL would support additional safeguards to ensure that volume based discounts in fact benefit the consumer.

Lender Representatives

MBA commended the proposal to clarify the legality of volume based discounts, but said that it did not go far enough. MBA stated that negotiated discount arrangements for services and materials result in lower costs for consumers and are consistent with RESPA's purposes of lowering settlement costs. MBA stated, however, that by including a requirement that no more than the reduced price can be charged to the borrower, there will be little incentive for lenders to enter into discount arrangements. MBA stated that scrutiny to ensure that each and every dollar of discount is passed on to the consumer presents regulatory risks and will make the exception "uninviting." MBA asserted that such a restriction is unnecessary, since market competition will result in the consumer receiving the benefit of the discounts. MBA also questioned the idea that discounts can be negotiated only by a settlement service provider, arguably excluding builders. MBA stated that such an approach could deprive consumers of negotiated discounts on house prices offered by lenders that have joint ventures and marketing agreements with builders.

The ABA and the Independent Community Bankers of America (ICBA) expressed concern that volume discounts may put smaller market participants such as community banks at a disadvantage, since most discounts will be negotiated on a volume basis. According to these commenters, smaller banks, making fewer loans, will not be able to negotiate as many or as deep discounts as larger lenders. ABA also commented

that lenders should be allowed to benefit as well from negotiated discounts by not being required to pass along the entire savings to the borrower, or there is little incentive for them to enter into such arrangements.

CMC supported the proposal to clarify the legality of negotiated discounts and stated that the proposed change to the regulations would be most likely to lead to greater competition and lower overall prices in situations where the lender or other party negotiating the discount absorbs the cost of the negotiated service and does not pass on the cost to the borrower. CMC stated that a clarification that a negotiated discount would not constitute a thing of value in this situation would provide greater flexibility to negotiate lower prices. CMC urged HUD to clarify that the clarification should not be limited to discounts negotiated by settlement service providers, but should also apply to parties who may not be regarded as settlement service providers such as builders. In addition, CMC stated that HUD should allow the discounted price charged to the borrower to be calculated on an average cost price basis.

Other Commenters

ALTA and other title industry commenters stated that allowing settlement service providers to negotiate volume based discounts would be anticompetitive and disproportionately harm small businesses. ALTA stated that the ability to negotiate volume discounts on the local services that are incidental to the issuance of a title policy (such as a title search) will disadvantage the small title insurance agency that does not have the resources to guaranty a stream of business to a third party or discount its own services when the services are performed in-house. In addition, ALTA expressed concern that mortgage lenders and brokers will add to the anticompetitive effects by

favoring affiliated title companies or those companies that can provide title related services on a nationwide basis. ALTA asserted that the Regulatory Impact Analysis of the proposed rule did not adequately address these issues.

ALTA also noted that although the proposed rule would allow settlement service providers to offer negotiated volume discounts, such a provision is in direct contrast to many state title insurance laws that prohibit title insurance companies and agencies from discounting the title premium or offering a rebate on title insurance fees, especially in states with "all-inclusive" rates. Similarly, the National Association of Insurance Commissioners (NAIC) stated that volume based discounts would be a violation of several states anti-rebating laws. NAIC expressed its concern that the rule could be found to preempt state laws to the contrary. It recommended that the provision be withdrawn or that HUD clarify that the volume based discounts and average cost pricing provisions are not intended to preempt state law.

Representative Donald A. Manzullo of the U.S. House of Representatives expressed concern over volume based discounts, which he described as a "thinly veiled attempt to reintroduce the concept of 'bundling' services." The Congressman reiterated his previously stated concerns that the long term impact of volume discounts would eliminate competition and destroy small businesses. Rep. Manzullo stated that only large businesses have the resources necessary to determine the financial terms, negotiate for settlement services, or discount their own services. According to Rep. Manzullo, in order to compete, small businesses would be forced to reduce their prices and profit margins, driving many of them out of business. He stated that such an anticompetitive environment will allow large lenders to raise prices for settlement services.

Federal Agencies

The FDIC stated that it supports the requirement in the proposed definition of "thing of value" that no more than the discounted price may be charged to a borrower and disclosed on the HUD-1 form. In contrast, FTC staff stated that while it supports the removal of restrictions against volume based discounts, it believes that the proposed requirement to pass along the entire discount to the consumer will likely limit incentives to negotiate such discounts. According to FTC staff, requiring that 100 percent of any negotiated discount be passed on to customers reduces incentives of firms to spend resources to negotiate such discounts. FTC stated that the proposed regulation also does not clarify how to account for the overhead costs associated with price negotiation activities.

The Office of Advocacy of the Small Business Administration stated that pricing mechanisms such as volume based discounts potentially create an uneven playing field for small entities. This office reiterated concerns voiced by small businesses that volume based discounts will favor large settlement service providers at the expense of small business. According to the Office of Advocacy, some small entities may leave the market, which would ultimately result in a decrease in options and higher prices for consumers.

HUD Determination

HUD remains committed to a RESPA regulatory scheme that fosters mortgage settlement pricing mechanisms, that, as stated in the preamble to the March 2008 proposed rule "result in greater competition and lower costs to consumers" (73 FR at 14050). Nevertheless, given the comments received on the proposed change to HUD's

current regulatory definition of "thing of value" and the significant operational and other questions raised by the proposed change, HUD has decided to give further consideration beyond this rulemaking to a regulatory change that explicitly allows negotiated discounts, including volume based discounts, between loan originators and other settlement service providers and not to implement the proposed change at this time. HUD wants to ensure that any change will adequately protect consumers, while at the same time provide adequate market flexibility, and due consideration to small business concerns.

It remains HUD's position, however, that discounts negotiated between loan originators and other settlement service providers, or by an individual settlement service provider on behalf of a borrower, where the discount is ultimately passed on to the borrower in full, is not, depending upon the specific circumstances of a particular transaction, a violation of Section 8 of RESPA. If the borrower fully benefits from the discount, these types of mechanisms that lower consumer costs are within RESPA's principal purposes.

In addition to further rulemaking, HUD will consider other avenues for providing guidance on negotiated discounts, including through the issuance of statements of policy.

B. Methodology for Average Cost Pricing.

Proposed Rule. The March 2008 proposed rule would have permitted pricing techniques using average cost pricing. Under the proposed rule, settlement service providers who procure or who help consumers to obtain third party settlement services, would have been allowed to negotiate the pricing of those services by the third party provider. The proposed rule would have made clear that where average cost pricing is used, the evaluation of prices of third party services would focus on all of the loan

originator's transactions together, rather than viewing each transaction separately. An individual borrower might be charged more or less than the actual amount paid for that service in an individual transaction, provided that borrowers are being charged no more than the average price actually received by third parties during the period in which the average price is computed.

The proposed rule specified two methods that loan originators could use to calculate an average price for a particular settlement service. As set forth in the March 2008 proposed rule, the loan originator would designate a recent 6-month period as the "averaging period" for purposes of calculating the average price. The same average price would then have to be used in every transaction in that class of transactions for which a GFE is provided following the averaging period until a new averaging period is established. The average price would be calculated either as (1) the actual average price for the settlement service during the averaging period; or (2) a projected average under a tiered pricing contract, based on the number of transactions that actually closed during the recent averaging period. If a loan originator used one of these methods to calculate the average price for a settlement service, HUD would deem the loan originator to have complied with the requirements of the rule.

HUD invited comments on its proposed methods for calculating average cost prices and on any alternative methods that should be permitted. Specifically, HUD invited comments on how to define "class of transactions" and noted as an example that "class of transactions" could be defined by loan type or loan-to-value ratio. HUD also invited suggestions on alternative average cost pricing methods that benefit consumers and are based on factors that would lead to charges to the consumer (and the disclosure of

such charges) that are easily calculated, verified, and enforced, but difficult to manipulate in an abusive manner.

The March 2008 proposed rule provided that with regard to any pricing method used by a settlement service provider, if a violation of Section 8 of RESPA is alleged and an investigation ensues, the burden would be on the targeted settlement service provider to demonstrate compliance with a permissible pricing method through the production of relevant records.

Comments

Consumer Representatives

NCLC and CRL supported the concept of average cost pricing but expressed concern that the proposed rule used the terms "average pricing" and "average cost pricing" interchangeably. These commenters stated that "average cost pricing" must be based on the cost of the settlement service and established rate of return for the settlement service provider. They expressed concern that the proposed rule appeared to allow to "average pricing" whereby an originator charges the consumer an average cost while paying the third party settlement provider a different amount for each consumer. According to these commenters, there is no reason that the originator should not charge the consumer the actual cost of the third party service and reflect such cost on the HUD-1.

NCLC stated that the current description of acceptable methods for average cost pricing are inaccurate and should either be eliminated or revised to comport with true average cost pricing formulas. CRL stated that average cost pricing is inappropriate for certain costs that are partially dependent on loan amount, such as title insurance

premiums, recording costs, and transfer taxes, since average cost pricing would disadvantage those consumers purchasing or refinancing less expensive homes.

Lender Representatives

MBA supported the proposal to allow average cost pricing with some modifications and clarifications. MBA suggested, in addition to the approaches provided in the proposal, that the rule include another approach or approaches that would be less restrictive and facilitate entry into average cost pricing for other firms in order to benefit consumers. MBA recommended an approach whereby a firm would charge the average cost for a class of transactions over a prospective averaging period, during which all transactions in the class would be charged a projected average price. Under this approach, as long as the total amounts charged on transactions in the class do not exceed the amount paid to the service providers for such transactions by more than a small amount, the average price would be permissible.

MBA also recommended that a lender should be given maximum latitude to define a "class of transactions" based on type of service, type of property, loan type and/or geographic region. According to MBA, the lender should also have latitude to define an "average period" and the "average price" as long as the approach is "reasonable." MBA also recommended that the documentation requirements be revised to ensure that they are flexible and do not impede use of the provision by requiring unnecessary burdensome documentation.

CMC supported the proposal to allow average cost pricing, and stated that such a provision could lead to flexible negotiations for settlement services, thereby increasing price competition and lowering costs to borrowers. However, CMC stated that unless

such a proposal provides relief from liability under Section 8 of RESPA, there will be little incentive for loan originators or other settlement service providers to use average cost pricing. CMC also stated that placing the burden of demonstrating compliance on the settlement service provider is problematic. CMC stated that the two methods set forth in the proposed rule for calculating an average price leave open questions as to compliance and workability. According to CMC, since circumstances often change, the approach set forth in the proposal for determining the averaging period may not be practical.

CMC recommended that a simpler method would be to let the provider who will charge the average cost define the class of transactions and a prospective averaging period during which all transactions in the class would be charged a projected average price. CMC also recommended that as long as the total amounts charged on transactions in the class do not exceed the amount paid to the service providers for such transactions by more than a small amount, such as by more than 10 percent, the average price should be permissible. CMC recommended an averaging period of up to 18 months since many contracts are reviewed on an annual basis and there are seasonal variations in volume. With respect to how the class of transactions should be determined, CMC recommended that HUD not specify a set of factors for use in determining class of transactions, but rather, allow a settlement service provider to define the class in any reasonable manner. CMC also urged HUD to clarify that prices may be uniformly reduced at any point during the averaging period to ensure that the total costs charged on the transactions remain within the applicable tolerance.

In addition, CMC urged HUD to clarify that average cost pricing may be used in situations where there is more than one settlement service provider. CMC stated that the exemption for average cost pricing will be of limited value unless such pricing is available when multiple providers are providing the same service and the fees charged by these providers vary. CMC also urged HUD to coordinate with the Federal Reserve Board regarding how average cost pricing affects the calculation of the finance charge for purposes of TILA. Finally, CMC recommended that HUD clarify that the average cost pricing provision is not limited to loan originators.

Other Commenters

RESPRO expressed support for average cost pricing and recommended that the rule clarify that average cost pricing is not limited to loan originators. In addition, RESPRO stated that the proposed approaches for average cost pricing need clarification. For example, RESPRO suggested that HUD clarify what constitutes a "recent" 6- month period and also clarify whether a loan originator can divide up its service territory into two or more geographical areas and utilize these areas for averaging purposes.

ALTA expressed support for the average cost pricing proposal and requested HUD to clarify that average cost pricing would be available for all settlement service providers. ALTA maintained that the proposed provision on average cost pricing should not have been included in the HUD-1 section of the RESPA regulations, but rather, should have been written so as to permit lenders and others to apply average cost pricing without running the risk of violating Section 8(b) of RESPA. Accordingly, ALTA urged HUD to clarify that average cost pricing is not a violation of Section 8(b). ALTA stated that if the rule would allow title and settlement companies to use the average cost price,

particularly as such pricing relates to recording fees, express delivery charges, and other third party charges for which title companies must pay, consumers would benefit from the certainty the average cost provides, and that the threat of class action litigation for title and settlement companies with respect to recording fees would be removed.

NAR stated that average cost pricing should be allowed for both borrowers and sellers, and should be extended to all settlement service providers. NAR stated that average cost pricing should be limited to small items such as courier fees and recording costs. According to NAR, if average cost pricing is allowed for larger items such as appraisals, the consumer will end up paying more for an "average cost" if, for example, the calculation includes a disproportionate number of expensive appraisals during a given 6-month period.

CSBS, AARMR, and NACCA commented that the proposal to allow loan originators or settlement service providers to utilize average cost pricing would be difficult for regulators to enforce and recommended that the burden of proof of compliance be placed on the lender. These commenters stated that by allowing loan originators and providers to utilize this pricing mechanism, individual transaction costs could be manipulated and inflated. These commenters noted that the current regulations can be enforced by regulators, because actual prices can be determined.

Federal Agencies

The FDIC expressed concern with the average cost pricing proposal on several grounds. First, the FDIC indicated that it is not aware of an appropriate means of evaluating whether overall consumer costs would decline as a result of average cost pricing. Second, the agency noted that even if some borrowers' settlement services costs

are reduced under average cost pricing, other borrowers will pay more for a service than is warranted for their particular loan. Third, the FDIC stated that the proposal does not include controls to ensure fairness, such as whether the lender calculated the average costs appropriately.

FTC staff stated that it supports average cost pricing but recommended that HUD consider eliminating restrictions on how average costs may be calculated. FTC staff stated that it supports removing barriers to average cost pricing because there is "no economic justification for requiring that each consumer pay his or her unique marginal cost of receiving settlement services and because doing so will likely result in lower prices for consumers." FTC staff added that calculating and maintaining records of such individualized costs and prices adds additional accounting and recordkeeping costs to the transaction that are not required in other competitive markets. FTC staff asserted that by removing such costs, the market will be more efficient and the result will be lower prices for consumers.

HUD Determination

Based on the comments received in response to the proposed rule, HUD has revised the average cost pricing provisions to provide more flexibility and greater clarity.

Commenters representing some consumer interests opposed implementation of the proposed average cost pricing provision, recommending that HUD limit charges for third party services to the actual cost of providing those services, plus an established rate of return. While HUD appreciates these comments, the proposed average cost pricing provision was not intended to limit the amounts charged for settlement services in this fashion, but instead simply provided for an alternative means of calculating and

disclosing settlement charges on the HUD-1 or HUD-1A settlement statements. In order to avoid similar confusion about the intent of this provision in the future, the final rule uses the term "average charge" in place of "average cost pricing." The term "average charge" appropriately focuses on the amount disclosed on the settlement statement, rather than the underlying costs of providing a particular settlement service.

The final rule also clarifies that an average charge may be used by any settlement service provider that obtains a service from a third party on behalf of a borrower or seller; the provision is not limited to loan originators. HUD has determined that benefits to consumers and the benefits of reduced recordkeeping requirements and pricing flexibility from this provision should not be limited to one group of settlement service providers. Any provider that is able to calculate an average charge for a service in accordance with this provision and that is able to meet the provision's recordkeeping requirements is permitted to use an average charge for that service.

In addition to these clarifying changes, HUD has made several other significant changes to provide additional flexibility in calculating average charges. HUD has determined that its objective of providing a method that benefits consumers and results in charges that are easily calculated, verified, and enforced is best served by restricting the actual charges imposed on borrowers and sellers rather than by prescribing a particular method for calculating those charges.

The final rule provides that an average charge may be used for any settlement service, provided that the total amounts received from borrowers for that service for a particular class of transactions do not exceed the total amounts paid to the providers of that service for that class of transactions. This approach leaves the method of

determining the average charge to the discretion of the settlement service provider. However, the provider must ensure that the average charge used does not result in borrowers, in the aggregate, paying more for a particular settlement service than the aggregate price paid for obtaining that service from third parties. HUD has determined that this approach balances the settlement service provider's interest in flexibility in calculating an average charge with the borrower's interest in preventing excessive settlement charges. This approach is intended to promote greater efficiencies that ultimately lead to lower prices for consumers.

The final rule provides that a settlement service provider may define a class of transactions based on the period of time, type of loan, and geographic area. For example, a settlement service provider might calculate an average charge for all purchase money mortgages in the States of Georgia and South Carolina in a specified period of time. Alternatively, a settlement service provider could establish the class of transactions in which it would use a single average charge broadly, e.g., all transactions it engages in for a period of time, regardless of loan type or location. The settlement service provider must recalculate the average charge at least every 6 months. In order to prevent selective use of an average charge, the final rule provides that if an average charge is used in any class of transactions defined by the settlement service provider, then that provider must use the same average charge for every transaction within that class.

The final rule also prohibits the use of average charges for settlement services where the charge is based on the loan amount or the value of the property. Permitting average charges for those types of services would require borrowers in transactions with lower loan amounts and property values to subsidize the costs for borrowers with higher

loan amounts and property values. HUD has determined that such subsidization is not in the interest of consumers. This prohibition applies to charges such as transfer taxes, daily interest charges, reserves or escrow, and all types of insurance, including mortgage insurance, title insurance, and hazard insurance.

The final rule maintains the proposed recordkeeping requirements, to ensure that average charges are calculated appropriately and that regulators and borrowers are able to determine the basis on which the average charge was determined. Any settlement service provider that uses an average charge for a particular service must maintain all documents that were used to calculate the average charge for at least three years after any settlement in which the average charge was used.

VI. Prohibition Against Requiring the Use of Affiliates – Discussion of Public Comments

Proposed Rule. Under the March 2008 proposed rule, the current definition of "required use" in 24 CFR 3500.2 would be changed so that consumers would be more likely to shop for the homes and home features, and the loans and settlement services, that are best for them, free from the influence of deceptive referral arrangements. Through this proposed change, HUD sought to establish that in a real estate transaction covered by RESPA, incentives that consumers may want to accept and disincentives that consumers may want to avoid should be analyzed similarly for compliance with RESPA.

The proposed change would have made clear that HUD views economic disincentives that a consumer can avoid only by purchasing a settlement service from particular providers, or from businesses to which the consumer has been referred, to be potentially as problematic under RESPA as are economic incentives that are contingent

on the consumer's choice of a particular settlement service provider. The modifications in the proposed rule, however, were not intended to prevent discounts that are beneficial to consumers. The proposed definition stated that the offering by a settlement service provider of an optional package or combination of bona fide settlement services to a borrower at a total price lower than the sum of the prices of the individual settlement services would not constitute a "required use."

The proposed revision to the "required use" definition would have continued to apply in two sections of the regulations: the affiliated business exemption in 24 CFR 3500.15, and the prohibition on the seller requiring the buyer to purchase title insurance from a particular company in § 3500.16. However, in light of the other changes that would have been made by the proposed rule, the term "required use" would no longer have applied as it does currently in § 3500.7(e).

Comments

Consumer Representatives

NCLC stated that the proposed change to the "required use" definition does not go far enough to protect consumers. NCLC stated that the settlement services to obtain a home loan are only a small part of the costs of the loan. According to NCLC, the interest rate, the term of the loan, and whether a prepayment penalty is permitted, or a balloon payment is required, are all more important elements of the costs of the home loan than are the costs of settlement services. NCLC stated that "(i)t does not make sense for the settlement services to be capped in return for a required use, while the more critical components of the costs of the loan are not limited, especially where the service itself could be discounted while the loan terms are increased." NCLC proposed to define

"required use" to include the total cost of the loan in addition to the total of settlement services. CRL commended HUD's efforts in this area and agreed with NCLC that the definition of "required use" should include the total cost of the loan in addition to the cost of total settlement services.

The California Reinvestment Coalition supported the proposed change to the definition of "required use" and stated that the proposed change will "benefit the borrower by leveling the field."

Industry Representatives

Generally, lenders expressed opposition to the proposed change to the definition of "required use" on the grounds that the proposal is difficult to understand, is overbroad, and would eliminate the ability of builders and others to offer legitimate consumer discounts. MBA stated that it would be sufficient for HUD to indicate that under its current rules HUD may scrutinize discounts to assure that they are *bona fide,* rather than risking depriving borrowers of discounts altogether.

The ABA stated that the proposed change to the required use definition is "flawed and unreasonable" because HUD cited only anecdotal evidence that incentives have been abused by some companies to steer customers to affiliated vendors with high prices and inferior service, but offered "no empirical evidence to support this assertion." The ABA also stated that the proposal runs counter to the plain meaning of the words in the statute because defining "required use" to mean any incentive offered to use an affiliated company contradicts the unambiguous meaning of the statutory word "required." It stated that HUD should not confuse legitimate incentive arrangements among affiliated entities with undue influence or required use of a product or service.

NAMB, the Maryland Association of Mortgage Brokers (MAMB), and the Idaho Association of Mortgage Brokers (IAMB) expressed support for the proposed change in the definition of "required use." NAMB stated that the proposed revision should resolve the problems with tying and required use. NAMB recommended that the new definition avoid setting a threshold higher than zero for determining what constitutes an economic incentive or disincentive. NAMB, MAMB, and IAMB all stated that the threshold for determining incentives and disincentives should be "any thing of value."

Builders and builder-affiliated mortgage companies opposed the proposed change to the "required use" definition. CTX Mortgage Company asserted that the proposed change would "provide a significant road block for future customers to benefit from the streamlined mortgage and title services that Centex offers." The National Association of Home Builders (NAHB) asserted that the change would eliminate *bona fide* incentives, denying consumers significant savings in their home purchases. NAHB characterized HUD's examples of "required use" problems as "ambiguous and incomplete." NAHB asserted that home builders with affiliated lenders have business incentives to ensure that home buyers are pleased with the experience of obtaining loans from their affiliated lenders. NAHB noted that studies of builder-affiliated mortgage companies conducted by an independent research firm have found that such firms have lower per-loan operating costs as compared to outside lenders. According to NAHB, while the savings from these economies and the other affiliate benefits are difficult to quantify, they are significant and are passed along to consumers in the form of incentives for use of a builder affiliate. NAHB stated that home builders in general do not increase the selling price of homes to offset these incentives and asserted that the vast majority of builders who provide

incentives for buyer use of affiliates do so in a responsible manner that brings substantial benefits to consumers. NAHB and other commenters also suggested alternative language to the proposed definition to ensure that consumers are presented with the option to select an incentive that is *bona fide*.

RESPRO objected to the proposed change to "required use" and stated that it would "prohibit many consumer incentives offered by home builders and real estate brokers in today's marketplace that provide consumers with lower costs and/or better service; is based on unsubstantiated and anecdotal evidence about alleged abuses; attempts to address violations that already are prohibited under RESPA, and is based on an inaccurate reading of anti-trust laws." RESPRO asserted that consumer incentives are offered to ensure that sales transactions close as quickly and as efficiently as possible. RESPRO recommended that the current definition of "required use" be retained.

NAR opposed the proposed change and stated that it would have at least two unintended consequences. According to NAR, the rule authorizes discounts only on the prices of the recommended provider and this would limit the kind of non-price/services promotions that joint venture owners currently and permissibly offer to promote affiliates. NAR noted that real estate agents and brokers offer a variety of inducements to clients to promote their services, such as by offering a gift certificate to a local business or a free home inspection. NAR indicated that it does not believe that HUD intended to eliminate a practice which benefits consumers. In addition, according to NAR, the proposal would allow a discounted combination of settlement services only to a borrower, and NAR believes that sellers should not be precluded from receiving

discounts as incentives as sellers often pay the majority of settlement costs in a real estate transaction.

Other Commenters

The Laborers' International Union of North America (LIUNA) supported the proposed change to the "required use" definition, stating that it "will promote more comparison shopping by borrowers and achieve HUD's intended goal of protecting consumers from unnecessarily high settlement costs."

LIUNA further stated that the "cost to the builders of incentives has already been built into the sales price, so that it is not a true discount, but a penalty for using another company." According to LIUNA, its research indicates that the effect of incentives "dissuade customers from comparison shopping for lenders." Rather, "customers are steered to loans that are very often more expensive, despite the incentives." LIUNA asserted that builders have improperly used "related business relationships at the expense of consumers" that "resulted in higher costs for homebuyers … and have played a large part in creating the current housing crisis." LIUNA provided statistics indicating that in February 2006, the average rate for a 30-year fixed-rate mortgage was 6.25 percent. In contrast, LIUNA noted that although the main benefit of an ARM is that it has a lower starting interest rate than the equivalent fixed-rate loan, approximately half of the mortgages made by certain builders in February 2006 were ARMs that had starting rates of 6.25 percent or higher. LIUNA stated that builders "have an incentive to sell their inventory at the highest possible price, and in-house mortgage units provide the financing to make it possible. There is evidence that during the housing boom in 2004-2006 builders were only able to sell homes at such inflated prices because of the collaboration

with their mortgage subsidiary and an affiliated appraisal company. This resulted in large numbers of homeowners who were "underwater," owing more than the value of their home, from day one."

CSBS, AARMR, and NACCA supported the proposed change to the "required use" definition. However, these commenters recommended that the definition of "required use" be expanded to incorporate situations where the originator fails to give a required Affiliated Business Arrangement disclosure, or provides a misleading disclosure that facilitates steering of the borrower to an affiliate. According to these commenters, absent information necessary to make the best decision, the borrower has effectively been required to use a particular provider.

The FTC staff recommended that HUD reconsider the proposed change to the definition of required use. The FTC staff stated that the expanded definition could deprive customers of the lower prices that can result from bundling related services.

HUD Determination

After reviewing comments about HUD's proposal to change the definition of "required use" and re-examining aspects of the proposed revised definition, HUD has determined to retain the concepts in the definition of "required use" set forth in the proposed rule, but with some revisions that better reflect HUD's intent in applying the definition. The new definition makes it clear that economic disincentives that are used to improperly influence a consumer's choices are as problematic under RESPA as are incentives that are not true discounts. The revisions made in the definition subsequent to the proposed rule clarify how the definition will apply in the context of the affiliated

business exemption under Section 8(c) of RESPA and § 3500.15 of HUD's regulations, and similarly frames the definition to apply to "persons" rather than only "borrowers."

The change to the definition of "required use" will not eliminate the ability of anyone to offer legitimate consumer discounts. HUD does not interpret RESPA as preventing a settlement service provider or anyone else from offering a discount or other thing of value directly to the consumer. However, RESPA and this final rule limit tying such a discount to the use of an affiliated settlement service provider. HUD believes that consumers will utilize affiliated and preferred businesses if the costs of using those businesses are lower than the costs associated with similar services from other providers. Similarly to the proposed rule, the final rule continues to provide that settlement service providers can offer " a combination of bona fide settlement services at a total price (net of the value of the associated discount, rebate, or other economic incentive) lower than the sum of the market prices of the individual settlement services and will not be found to have required the use of the settlement service providers as long as: (1) the use of any such combination is optional to the purchaser; and (2) the lower price for the combination is not made up by higher costs elsewhere in the settlement process."

VII. Technical Amendments

Proposed Rule

The March 2008 proposed rule included several changes to HUD's regulations to reflect current statutory provisions. First, the proposed rule revised the mortgage servicing disclosure requirements in 24 CFR 3500.21 to be consistent with section 2103 of the Economic Growth and Regulatory Paperwork Reduction Act of 1996 (Title II of the Omnibus Consolidated Appropriations Act, 1997) (Pub. L. 104-208) and sought

public comment on whether the mortgage servicing disclosure should be included as part of the GFE.

Second, the proposed rule eliminated outdated provisions regarding the phase-in period for aggregate accounting for escrow accounts in 24 CFR 3500.17. The phase-in period ended October 27, 1997. Eliminating those provisions of the codified RESPA regulations that are no longer applicable to the home settlement process simplifies and clarifies the rules for escrow accounts.

Finally, the March 2008 proposed rule would add a new § 3500.23 to make clear that the electronic disclosures permitted pursuant to the Electronic Signatures in Global and National Commerce Act (ESIGN) (15 U.S.C. 7001-7031) apply to all disclosures provided for in HUD's RESPA regulations.

Comments

Almost all of the comments that addressed the proposed technical changes to the rule expressed support for these changes. Several lenders and trade groups representing lenders and mortgage brokers commented favorably on the changes that conform the transfer of servicing disclosure regulations to the revised statutory requirements. However, lenders and their trade groups were generally opposed to including the transfer of servicing disclosure on the revised GFE.

Several groups representing consumer interests commented on the transfer of servicing regulation, and strongly supported expanding the transfer of servicing regulations beyond first lien mortgage loans. These groups indicated that the TILA regulations, which HUD cited as the basis for excluding subordinate lien mortgage loans from the transfer of servicing disclosure requirements, do not provide equivalent

protections, and that the transfer of servicing requirements should therefore be expanded to cover all federally related mortgage loans. Consumer groups also recommended changes to the language used in the proposed revision to the transfer of servicing disclosure. The consumer group commenters indicated that the disclosure's description of the servicing function is unrealistically narrow, and that it should be revised to state that:

> Servicers are responsible for account maintenance activities such as sending monthly statements, accepting payments, keeping track of account balances, handling escrow accounts, engaging in loss mitigation and prosecuting foreclosures. They handle interest rate adjustments on adjustable rate mortgages, collect and report information to national credit bureaus, and remit monies to the owners of the loan.

Very few comments were received on the proposed revisions to the escrow accounting regulations, or on the proposed clarification regarding the applicability of ESIGN to RESPA. The comments that were received on these changes were primarily from trade groups representing lenders and mortgage brokers, and the comments were limited to general expressions of support for the changes proposed.

HUD Determination

Based on the comments received, HUD has determined that the changes to the transfer of servicing requirements should be included in the final rule. These changes conform HUD's regulations to the revised statutory requirements, and resolve any questions about whether lenders must still follow the outdated provisions. No commenters raised objections to the changes proposed; the most substantial comments

received were from consumer groups that advocated expanding the coverage of the transfer of servicing requirements. In light of the numerous comments from lenders and those trade groups representing lenders that opposed inclusion of the transfer of servicing disclosure on the GFE, HUD has determined not to include that disclosure on the revised GFE at this time. However, HUD is not expanding the coverage of the transfer of servicing regulations at this time. While HUD may consider doing so at a later time, significantly expanding the coverage of the transfer of servicing regulations would be beyond the scope of the technical amendments in the proposed rule and would likely require additional comment from affected parties.

The language on the revised model transfer of servicing disclosure form has been modified somewhat from the proposed rule in light of the comments received. The transfer of servicing disclosure form is not intended to provide a comprehensive list of all functions that might be performed by any servicer, but HUD agrees with those commenters that suggested that the description of the functions performed by servicers was too narrow. Accordingly, HUD has revised that sentence on the form to provide a more accurate description of the functions performed by loan servicers.

HUD has also determined that the proposed elimination of the phase-in period for aggregate accounting for escrow accounts should be included in the final rule. This change simply eliminates a regulatory provision that is no longer applicable. The only significant comments HUD received on this provision were in favor of making the change proposed.

Finally, HUD has determined that the new provision clarifying the applicability of ESIGN to RESPA should also be included in the final rule. While the electronic methods

of disclosure permitted pursuant to ESIGN could be used for disclosures required under RESPA, even in the absence of this regulatory clarification, this provision will allay any doubts that industry participants may have had about the permissibility of electronic disclosures under RESPA. The only significant comments HUD received on this provision were in favor of making the proposed change.

VIII. Regulatory Flexibility Act – Comments of the Office of Advocacy of the Small Business Administration

As part of its statutory duty to review an agency's compliance with the Regulatory Flexibility Act (RFA), as amended by the Small Business Regulatory Enforcement Fairness Act (SBREFA), the Office of Advocacy of the U.S. Small Business Administration (Advocacy) reviewed the proposed rule and submitted its comments to the Department. In its letter of June 11, 2008, Advocacy expressed the concern that HUD may have underestimated the economic impact of the proposed rule on small entities. Advocacy indicated that it had met with a wide range of small entity representatives from different sectors of the industry and several of these representatives indicated that the proposed rule would have a greater economic impact than the $548 million in annual recurring compliance costs for small businesses as stated by HUD in the Economic Analysis accompanying the proposal. Accordingly, Advocacy advised HUD to document the additional costs to small businesses.

In addition, Advocacy expressed the following concerns about the proposed rule: (1) the proposed rule's tolerance levels may be problematic for loan originators because some settlement costs can change on a daily basis, making the loan originator responsible for the actions of a third party beyond its control; (2) the proposed rule's requirement that

a closing script be read to the borrower at the closing will present problems for small entities; (3) the proposal to allow volume discounts will favor large settlement service providers and loan originators at the expense of small businesses; and (4) the proposed rule's characterization of YSP as a credit to the borrower will put mortgage brokers at a competitive disadvantage compared to lenders, and may create confusion among borrowers. Advocacy supported moving forward without the closing script requirement, the volume discount language, and the yield spread premium classification. In addition, Advocacy recommended that HUD clarify the provision on tolerances and encouraged HUD to provide a delay in the implementation date in the final rule to allow small businesses the opportunity to absorb the costs and comply with the new requirements.

HUD carefully considered the comments provided by Advocacy and certain modifications have been made in the final rule that address Advocacy's concerns. For example, the Department has determined not to adopt the closing script requirement set forth in the proposed rule. In addition, the proposed rule language explicitly allowing negotiated discounts, including volume based discounts between loan originators and other settlement service providers, has not been included in the final rule. HUD also revised a number of provisions on tolerances and clarified the situations where a loan originator would no longer be bound by the tolerances.

With respect to the characterization of YSP as a credit to the borrower, HUD has designed and tested the GFE form to enable borrowers to accurately determine the lowest cost loan. Testing of the GFE indicated no bias in the selection of loans with lowest settlement cost, between "broker" loans (YSP reported) and "lender" loans (no YSP reported).

With respect to statements in the Economic Analysis for the RESPA proposed rule concerning cost impacts of the rule on small businesses, HUD recognizes that there will be one-time adjustment costs and recurring costs on small businesses. Once incurred, the adjustment costs will not be incurred again. Thus, combining recurring and adjustment costs would be an accurate measure for the burden of the rule during the first year only. The recurring costs per loan are equivalent for small and large businesses. The aggregate recurring compliance cost depends on loan volume and is not underestimated for small businesses relative to large businesses. Advocacy and some other commenters questioned aspects of the cost estimates of the rule, but did not provide alternative cost estimates supported by data. HUD carefully considered an alternative analysis prepared for NAR that was not based on new data. HUD accepted and implemented suggestions in this analysis to perform a sensitivity analysis of the ratio of applications per loan in its Final Regulatory Flexibility Analysis.

With respect to Advocacy's recommendation that HUD allow a longer implementation period to mitigate the cost burden associated with the new requirements on small businesses , HUD has determined that a one-year implementation period is sufficient to make the transition to the new requirements. Many commenters agreed. Instituting a longer implementation period for small businesses would significantly weaken the effective and orderly implementation of the new rule. Allowing small firms to operate under different rules would create confusion in the closing of loans, especially in transactions that involve both large and small firms.

IX. Findings and Certifications

Paperwork Reduction Act

The information collection requirements contained in this rule were submitted to the Office of Management and Budget (OMB) under the Paperwork Reduction Act of 1995 (44 U.S.C. 3501-3520), and were assigned OMB control number 2502-0265. In accordance with the Paperwork Reduction Act, an agency may not conduct or sponsor, and a person is not required to respond to, a collection of information, unless the collection displays a currently valid OMB control number.

Environmental Impact

A Finding of No Significant Impact with respect to the environment was made at the proposed rule stage in accordance with HUD regulations at 24 CFR part 50, which implement section 102(2)(C) of the National Environmental Policy Act of 1969 (42 U.S.C. 4332(2)(C)). That finding remains applicable to this final rule and is available for public inspection between the hours of 8:00 a.m. and 5:00 p.m. weekdays in the Regulations Division, Office of General Counsel, Department of Housing and Urban Development, 451 7th Street, SW, Room 10276, Washington, DC 20410-0500. Due to security measures at the HUD Headquarters building, an advance appointment to review the finding must be scheduled by calling the Regulations Division at 202-402-3055 (this is not a toll-free number). Individuals with speech or hearing impairments may access this number through TTY by calling the Federal Information Relay Service at 800-877-8339.

Executive Order 12866, Regulatory Planning and Review

The Office of Management and Budget (OMB) reviewed this rule under Executive Order 12866 (entitled "Regulatory Planning and Review"). This rule was determined economically significant under the executive order.

There is strong evidence of information asymmetry between mortgage originators and settlement service providers and consumers. This information asymmetry allows loan originators and settlement service providers to capture much of the consumer surplus in this market by charging different prices to similar consumers for similar products, a process economists call price discrimination. The RESPA disclosure statute is meant to address this information asymmetry, but the evidence shows that the current RESPA regulations have not provided consumers necessary information in a way they can use effectively.

The final rule will create a more level-playing field through a more transparent and standard disclosure of loan details and settlement costs; tolerances on settlement charges leading to prices that consumers can rely on; and adding a comparison page to the HUD-1 that allows the consumer to compare the amounts listed for particular settlement costs on the GFE with the total costs listed for those charges on the HUD-1, and to double check the loan details at settlement. These changes will encourage comparison shopping by informed consumers, which will place a competitive pressure on market prices, and enable consumers to benefit.

It is estimated that borrowers will save $8.35 billion annually in origination and settlement charges. This transfer to borrowers from price-discriminating producers

constitutes 12.5 percent of total charges, and represents consumer savings of $668 per loan with a range between $500 and $700 per loan.

The total one-time adjustment costs to the lending and settlement industry of the proposed GFE and HUD-1 are estimated to be $570 million, or $46 per loan. Total recurring costs are estimated to be $918 million annually, or $74 per loan. Even if all of the adjustment and recurring costs of the rule were passed along to consumers, individual consumers would still enjoy substantial benefits. If all of the adjustment and recurrent costs are passed on to borrowers in the first year and no industry efficiency gains are passed to consumers, the net consumer savings for the average consumer in the first year would be $548 and $594 per loan every year afterwards.

In addition to the private benefits, there are far reaching social benefits. The lower profitability of seeking out less-informed borrowers for less-competitive loans should lead to a reduction in this non-productive activity. If the decline in this activity represented one percent of current loan originator effort, this would result in $420 million in social surplus. Another social benefit of the rule is its contribution to sustainable homeownership. Consumers who better understand the details of their loans, and save money on their and settlement costs, are more likely to avoid risky loans, default, and foreclosure. There are substantial negative economic externalities of a foreclosure to neighboring properties and local governments, as well as private costs to the borrower and lender. The size of this social benefit would be in addition to the other benefits enumerated in the Regulatory Impact Analysis.

The costs and benefits are discussed in more detail in the Regulatory Impact Analysis that accompanies this rule.

Any changes made to the rule subsequent to its submission to OMB are identified in the docket file, which is available for public inspection in the Regulations Division, Office of General Counsel, Department of Housing and Urban Development, 451 7th Street, SW, Room 10276, Washington, DC, 20410-0500. The Economic Analysis prepared for this rule is also available for public inspection in the Regulations Division. Due to security measures at the HUD Headquarters building, an advance appointment to review these items must be scheduled by calling the Regulations Division at 202-402-3055 (this is not a toll-free number). Individuals with speech or hearing impairments may access this number through TTY by calling the Federal Information Relay Service at 800-877-8339.

Federalism Impact

This rule does not have federalism implications and does not impose substantial direct compliance costs on state and local governments or preempt State law within the meaning of Executive Order 13132 (entitled "Federalism").

Regulatory Flexibility Act

The Secretary, in accordance with the Regulatory Flexibility Act (5 U.S.C. 605(b)), has reviewed and approved this rule and determined that the rule would have a significant economic impact on a substantial number of small entities within the meaning of the Regulatory Flexibility Act. In accordance with section 603 of the Regulatory Flexibility Act, a Final Regulatory Flexibility Analysis (FRFA) has been prepared. The FRFA is presented in an Appendix to this final rule and is included as Chapter 6 in the Regulatory Impact Analysis prepared under Executive Order 12866.

Unfunded Mandates Reform Act

Title II of the Unfunded Mandates Reform Act of 1995 (2 U.S.C. 1531-1538) (UMRA) requires federal agencies to assess the effects of their regulatory actions on state, local, and tribal governments and on the private sector. This rule does not, within the meaning of the UMRA, impose any federal mandates on any state, local, or tribal governments nor on the private sector.

Congressional Review of Final Rules

This rule constitutes a "major rule" as defined in the Congressional Review Act (5 U.S.C. Chapter 8). This rule has a 60-day delayed effective date and will be submitted to the Congress in accordance with the requirements of the Congressional Review Act.

List of Subjects

24 CFR part 203

Hawaiian Natives, Home improvement, Indians-lands, Loan programs-housing and community development, Mortgage insurance, Reporting and recordkeeping requirements, Solar energy

24 CFR part 3500

Consumer protection, Condominiums, Housing, Mortgagees, Mortgage servicing, Reporting, and Recordkeeping requirements.

For the reasons set out in the preamble, parts 203 and 3500 of title 24 of the Code of Federal Regulations are amended as follows:

PART 203 – SINGLE FAMILY MORTGAGE INSURANCE

1. The authority citation shall continue to read as follows:

Authority: 12 U.S.C. 1709, 1710, 1715b, 1715z-16, and 1715u; 42 U.S.C. 3535(d).

2. In § 203.27, paragraph (a)(2) is revised to read as follows:

§ 203.27 Charges, fees or discounts

(a) * * *

(2) A charge to compensate the mortgagee for expenses incurred in originating and closing the loan, *provided* that the Commissioner may establish limitations on the amount of any such charge.

PART 3500 – REAL ESTATE SETTLEMENT PROCEDURES ACT

3. The authority citation shall continue to read as follows:

Authority: 12 U.S.C. 1709, 1710, 1715b, 1715z-16, and 1715u; 42 U.S.C. 3535(d).

4. Section 3500.1 is revised to read as follows:

§ 3500.1 Designation and Applicability.

(a) *Designation*. This part may be referred to as Regulation X.

(b) *Applicability*. The following sections, as revised by the final rule published on November 17, 2008**,** are applicable as follows:

(1) The definition of *Required use* in § 3500.2, §§ 3500.8(b), 3500.17, 3500.21, 3500.22, and 3500.23, and Appendices E and MS-1 are applicable commencing January 16, 2009.

(2) Section 203.27, the definitions other than *Required use* in § 3500.2, § 3500.7, §§ 3500.8(a) and(c), § 3500.9, and Appendices A and C, are applicable commencing January 1, 2010.

5. In § 3500.2, paragraph (b) is amended by revising the definitions of *Application*, *Good faith estimate*, *Mortgage broker*, and *Required use,* and by adding, in

alphabetical order, the following new definitions of *Balloon payment*, *Changed circumstances*, *Loan originator*, *Origination service*, *Prepayment penalty*, *Third party*, *Title service*, and *Tolerance*, to read as follows:

§ 3500.2 Definitions.

* * * * *

(b) * * *

Application means the submission of a borrower's financial information in anticipation of a credit decision relating to a federally related mortgage loan, which shall include the borrower's name, the borrower's monthly income, the borrower's social security number to obtain a credit report, the property address, an estimate of the value of the property, the mortgage loan amount sought, and any other information deemed necessary by the loan originator. An application may either be in writing or electronically submitted, including a written record of an oral application.

Balloon payment has the same meaning as "balloon payment" under Regulation Z (12 CFR part 226).

Changed circumstances means: (1) (i) Acts of God, war, disaster, or other emergency;

(ii) Information particular to the borrower or transaction that was relied on in providing the GFE and that changes or is found to be inaccurate after the GFE has been provided. This may include information about the credit quality of the borrower, the amount of the loan, the estimated value of the property, or any other information that was used in providing the GFE;

(iii) New information particular to the borrower or transaction that was not relied on in providing the GFE; or

(iv) Other circumstances that are particular to the borrower or transaction, including boundary disputes, the need for flood insurance, or environmental problems.

(2) Changed circumstances do not include:

(i) The borrower's name, the borrower's monthly income, the property address, an estimate of the value of the property, the mortgage loan amount sought, and any information contained in any credit report obtained by the loan originator prior to providing the GFE, unless the information changes or is found to be inaccurate after the GFE has been provided; or

(ii) Market price fluctuations by themselves.

* * * * *

Good faith estimate or *GFE* means an estimate of settlement charges a borrower is likely to incur, as a dollar amount, and related loan information, based upon common practice and experience in the locality of the mortgaged property, as provided on the form prescribed in § 3500.7 and prepared in accordance with the Instructions in Appendix C to this part.

* * * * *

Loan originator means a lender or mortgage broker.

* * * * *

Mortgage broker means a person (not an employee of a lender) or entity that renders origination services and serves as an intermediary between a borrower and a lender in a transaction involving a federally related mortgage loan, including such a

person or entity that closes the loan in its own name in a table funded transaction. A loan correspondent approved under 24 CFR 202.8 for Federal Housing Administration programs is a mortgage broker for purposes of this part.

* * * * *

Origination service means any service involved in the creation of a mortgage loan, including but not limited to the taking of the loan application, loan processing, and the underwriting and funding of the loan, and the processing and administrative services required to perform these functions.

* * * * *

Prepayment penalty has the same meaning as "prepayment penalty" under Regulation Z (12 CFR part 226).

* * * * *

Required use means a situation in which a person's access to some distinct service, property, discount, rebate, or other economic incentive, or the person's ability to avoid an economic disincentive or penalty, is contingent upon the person using or failing to use a referred provider of settlement services. In order to qualify for the affiliated business exemption under § 3500.15, a settlement service provider may offer a combination of bona fide settlement services at a total price (net of the value of the associated discount, rebate, or other economic incentive) lower than the sum of the market prices of the individual settlement services and will not be found to have required the use of the settlement service providers as long as: (1) the use of any such combination is optional to the purchaser; and (2) the lower price for the combination is not made up by higher costs elsewhere in the settlement process.

* * * * *

Third party means a settlement service provider other than a loan originator.

* * * * *

Title service means any service involved in the provision of title insurance (lender's or owner's policy), including but not limited to: title examination and evaluation; preparation and issuance of title commitment; clearance of underwriting objections; preparation and issuance of a title insurance policy or policies; and the processing and administrative services required to perform these functions. The term also includes the service of conducting a settlement.

* * * * *

Tolerance means the maximum amount by which the charge for a category or categories of settlement costs may exceed the amount of the estimate for such category or categories on a GFE.

6. In § 3500.7, paragraphs (a) through (e) are revised; paragraph (f) is redesignated as paragraph (h); and new paragraphs (f), (g), and (i) are added, as follows:

§ 3500.7 Good faith estimate or GFE.

(a) *Lender to provide*. (1) Except as otherwise provided in paragraphs (a), (b), or (h) of this section, not later than 3 business days after a lender receives an application, or information sufficient to complete an application, the lender must provide the applicant with a GFE. In the case of dealer loans, the lender must either provide the GFE or ensure that the dealer provides the GFE.

(2) The lender must provide the GFE to the loan applicant by hand delivery, by placing it in the mail, or, if the applicant agrees, by fax, email, or other electronic means.

(3) The lender is not required to provide the applicant with a GFE if, before the end of the 3-business-day period:

(i) The lender denies the application; or

(ii) The applicant withdraws the application.

(4) The lender is not permitted to charge, as a condition for providing a GFE, any fee for an appraisal, inspection, or other similar settlement service. The lender may, at its option, charge a fee limited to the cost of a credit report. The lender may not charge additional fees until after the applicant has received the GFE. If the GFE is mailed to the applicant, the applicant is considered to have received the GFE 3 calendar days after it is mailed, not including Sundays and the legal public holidays specified in 5 U.S.C. 6103(a).

(5) The lender may at any time collect from the loan applicant any information that it requires in addition to the required application information. However, the lender is not permitted to require, as a condition for providing a GFE, that an applicant submit supplemental documentation to verify the information provided on the application.

(b) *Mortgage broker to provide*. (1) Except as otherwise provided in paragraphs (a), (b), or (h) of this section, either the lender or the mortgage broker must provide a GFE not later than 3 business days after a mortgage broker receives either an application or information sufficient to complete an application. The lender is responsible for ascertaining whether the GFE has been provided. If the mortgage broker has provided a GFE, the lender is not required to provide an additional GFE.

(2) The mortgage broker must provide the GFE by hand delivery, by placing it in the mail, or, if the applicant agrees, by fax, email, or other electronic means.

(3) The mortgage broker is not required to provide the applicant with a GFE if, before the end of the 3-business-day period:

(i) The mortgage broker or lender denies the application; or

(ii) The applicant withdraws the application.

(4) The mortgage broker is not permitted to charge, as a condition for providing a GFE, any fee for an appraisal, inspection, or other similar settlement service. The mortgage broker may, at its option, charge a fee limited to the cost of a credit report. The mortgage broker may not charge additional fees until after the applicant has received the GFE. If the GFE is mailed to the applicant, the applicant is considered to have received the GFE 3 calendar days after it is mailed, not including Sundays and the legal public holidays specified in 5 U.S.C. 6103(a).

(5) The mortgage broker may at any time collect from the loan applicant any information that it requires in addition to the required application information. However, the mortgage broker is not permitted to require, as a condition for providing a GFE, that an applicant submit supplemental documentation to verify the information provided on the application.

(c) *Availability of GFE terms*. Except as provided in this paragraph, the estimate of the charges and terms for all settlement services must be available for at least 10 business days from when the GFE is provided, but it may remain available longer, if the loan originator extends the period of availability. The estimate for the following charges are excepted from this requirement: the interest rate, charges and terms dependent upon the interest rate, which includes the charge or credit for the interest rate chosen, the adjusted origination charges, and per diem interest.

(d) *Content and form of GFE*. The GFE form is set out in Appendix C to this part. The loan originator must prepare the GFE in accordance with the requirements of this section and the Instructions in Appendix C to this part. The instructions in Appendix C to this part allow for flexibility in the preparation and distribution of the GFE in hard copy and electronic format.

(e) *Tolerances for amounts included on GFE*. (1) Except as provided in paragraph (f) of this section, the actual charges at settlement may not exceed the amounts included on the GFE for:

(i) The origination charge;

(ii) While the borrower's interest rate is locked, the credit or charge for the interest rate chosen;

(iii) While the borrower's interest rate is locked, the adjusted origination charge; and

(iv) Transfer taxes.

(2) Except as provided in paragraph (f) below, the sum of the charges at settlement for the following services may not be greater than 10 percent above the sum of the amounts included on the GFE:

(i) Lender-required settlement services, where the lender selects the third party settlement service provider;

(ii) Lender-required services, title services and required title insurance, and owner's title insurance, when the borrower uses a settlement service provider identified by the loan originator; and

(iii) Government recording charges.

(3) The amounts charged for all other settlement services included on the GFE may change at settlement.

(f) *Binding GFE*. The loan originator is bound, within the tolerances provided in paragraph (e) of this section, to the settlement charges and terms listed on the GFE provided to the borrower, unless a new GFE is provided prior to settlement consistent with this paragraph (f). If a loan originator provides a revised GFE consistent with this paragraph, the loan originator must document the reason that a new GFE was provided. Loan originators must retain documentation of any reasons for providing a new GFE for no less than 3 years after settlement.

(1) *Changed circumstances affecting settlement costs*. If changed circumstances result in increased costs for any settlement services such that the charges at settlement would exceed the tolerances for those charges, the loan originator may provide a revised GFE to the borrower. If a revised GFE is to be provided, the loan originator must do so within 3 business days of receiving information sufficient to establish changed circumstances. The revised GFE may increase charges for services listed on the GFE only to the extent that the changed circumstances actually resulted in higher charges.

(2) *Changed circumstances affecting loan*. If changed circumstances result in a change in the borrower's eligibility for the specific loan terms identified in the GFE, the loan originator may provide a revised GFE to the borrower. If a revised GFE is to be provided, the loan originator must do so within 3 business days of receiving information sufficient to establish changed circumstances.

(3) *Borrower-requested changes*. If a borrower requests changes to the mortgage loan identified in the GFE that change the settlement charges or the terms of the loan, the

loan originator may provide a revised GFE to the borrower. If a revised GFE is to be provided, the loan originator must do so within 3 business days of the borrower's request.

(4) *Expiration of original GFE*. If a borrower does not express an intent to continue with an application within 10 business days after the GFE is provided, or such longer time specified by the loan originator pursuant to paragraph (c) above, the loan originator is no longer bound by the GFE.

(5) *Interest rate dependent charges and terms*. If the interest rate has not been locked by the borrower, or a locked interest rate has expired, the charge or credit for the interest rate chosen, the adjusted origination charges, per diem interest, and loan terms related to the interest rate may change. If the borrower later locks the interest rate, a new GFE must be provided showing the revised interest rate-dependent charges and terms. All other charges and terms must remain the same as on the original GFE, except as otherwise provided in paragraph (f) of this section.

(6) *New home purchases*. In transactions involving new home purchases, where settlement is anticipated to occur more than 60 calendar days from the time a GFE is provided, the loan originator may provide the GFE to the borrower with a clear and conspicuous disclosure stating that at any time up until 60 calendar days prior to closing, the loan originator may issue a revised GFE. If no such separate disclosure is provided, the loan originator cannot issue a revised GFE, except as otherwise provided in paragraph (f) of this section.

(g) *GFE is not a loan commitment*. Nothing in this section shall be interpreted to require a loan originator to make a loan to a particular borrower. The loan originator is

not required to provide a GFE if the loan originator does not have available a loan for which the borrower is eligible.

* * * * *

(i) *Violations of section 5 of RESPA (12 U.S.C. 2604).* A loan originator that violates the requirements of this section shall be deemed to have violated section 5 of RESPA. If any charges at settlement exceed the charges listed on the GFE by more than the permitted tolerances, the loan originator may cure the tolerance violation by reimbursing to the borrower the amount by which the tolerance was exceeded, at settlement or within 30 calendar days after settlement. A borrower will be deemed to have received timely reimbursement if the loan originator delivers or places the payment in the mail within 30 calendar days after settlement.

7. **Section** 3500.8 is revised to read as follows:

§ 3500.8 Use of HUD-1 or HUD-1A settlement statements.

(a) *Use by settlement agent.* The settlement agent shall use the HUD–1 settlement statement in every settlement involving a federally related mortgage loan in which there is a borrower and a seller. For transactions in which there is a borrower and no seller, such as refinancing loans or subordinate lien loans, the HUD–1 may be utilized by using the borrower's side of the HUD–1 statement. Alternatively, the form HUD–1A may be used for these transactions. The HUD–1 or HUD–1A may be modified as permitted under this part. Either the HUD–1 or the HUD–1A, as appropriate, shall be used for every RESPA-covered transaction, unless its use is specifically exempted. The use of the HUD–1 or HUD–1A is exempted for open-end lines of credit (home-equity plans) covered by the Truth in Lending Act and Regulation Z.

(b) *Charges to be stated.* The settlement agent shall complete the HUD-1 or HUD-1A, in accordance with the instructions set forth in Appendix A to this part. The loan originator must transmit to the settlement agent all information necessary to complete the HUD-1 or HUD-1A.

(1) *In general*. The settlement agent shall state the actual charges paid by the borrower and seller on the HUD-1, or by the borrower on the HUD-1A. The settlement agent must separately itemize each third party charge paid by the borrower and seller. All origination services performed by or on behalf of the loan originator must be included in the loan originator's own charge. Administrative and processing services related to title services must be included in the title underwriter's or title agent's own charge. The amount stated on the HUD-1 or HUD-1A for any itemized service cannot exceed the amount actually received by the settlement service provider for that itemized service, unless the charge is an average charge in accordance with paragraph (b)(2) of this section.

(2) *Use of average charge*. (i) The average charge for a settlement service shall be no more than the average amount paid for a settlement service by one settlement service provider to another settlement service provider on behalf of borrowers and sellers for a particular class of transactions involving federally related mortgage loans. The total amounts paid by borrowers and sellers for a settlement service based on the use of an average charge may not exceed the total amounts paid to the providers of that service for the particular class of transactions.

(ii) The settlement service provider shall define the particular class of transactions for purposes of calculating the average charge as all transactions involving federally related mortgage loans for:

(A) A period of time as determined by the settlement service provider, but not less than 30 calendar days and not more than 6 months;

(B) A geographic area as determined by the settlement service provider; and

(C) A type of loan as determined by the settlement service provider.

(iii) A settlement service provider may use an average charge in the same class of transactions for which the charge was calculated. If the settlement service provider uses the average charge for any transaction in the class, the settlement service provider must use the same average charge in every transaction within that class for which a GFE was provided.

(iv) The use of an average charge is not permitted for any settlement service if the charge for the service is based on the loan amount or property value. For example, an average charge may not be used for transfer taxes, interest charges, reserves or escrow, or any type of insurance, including mortgage insurance, title insurance, or hazard insurance.

(v) The settlement service provider must retain all documentation used to calculate the average charge for a particular class of transactions for at least 3 years after any settlement for which that average charge was used.

(c) *Violations of section 4 of RESPA (12 U.S.C. 2604).* A violation of any of the requirements of this section will be deemed to be a violation of section 4 of RESPA. An inadvertent or technical error in completing the HUD-1 or HUD-1A shall not be deemed

a violation of section 4 of RESPA if a revised HUD-1 or HUD-1A is provided in accordance with the requirements of this section within 30 calendar days after settlement.

8. In § 3500.9, paragraph (a)(1) is revised as follows:

§ 3500.9 Reproduction of settlement statements.

(a) * * *

(1) The person reproducing the HUD–1 may insert its business name and logo in section A and may rearrange, but not delete, the other information that appears in section A.

* * * * *

9. Section 3500.17 is amended:

a. In paragraph (b) by removing the definitions of *Acceptable accounting method*, *Conversion date*, *Phase-in period*, *Post-rule account,* and *Pre-rule account*;

b. In paragraph (c) by revising the heading and paragraphs (c)(4), (5), (6), and (8);

c. By removing paragraph (d)(2);

d. By redesignating paragraphs (d) introductory text and (d)(1) as paragraphs (d)(1) and (d)(2);

e. By adding a new heading to paragraph (d) and by revising newly designated (d)(1) and (d)(2) introductory text; and

f. By removing paragraph (e)(3), to read as follows:

§ 3500.17 Escrow accounts.

* * * * *

(c) *Limits on payments to escrow accounts.* * * *

(4) *Aggregate accounting required*. All servicers must use the aggregate accounting method in conducting escrow account analyses.

(5) *Cushion*. The cushion must be no greater than one-sixth (1/6) of the estimated total annual disbursements from the escrow account.

(6) *Restrictions on pre-accrual*. A servicer must not practice pre-accrual.

* * *

(8) *Provisions in mortgage documents*. The servicer must examine the mortgage loan documents to determine the applicable cushion for each escrow account. If the mortgage loan documents provide for lower cushion limits, then the terms of the loan documents apply. Where the terms of any mortgage loan document allow greater payments to an escrow account than allowed by this section, then this section controls the applicable limits. Where the mortgage loan documents do not specifically establish an escrow account, whether a servicer may establish an escrow account for the loan is a matter for determination by other Federal or State law. If the mortgage loan document is silent on the escrow account limits and a servicer establishes an escrow account under other Federal or State law, then the limitations of this section apply unless applicable Federal or State law provides for a lower amount. If the loan documents provide for escrow accounts up to the RESPA limits, then the servicer may require the maximum amounts consistent with this section, unless an applicable Federal or State law sets a lesser amount.

* * *

(d) *Methods of escrow account analysis.* (1) The following sets forth the steps servicers must use to determine whether their use of aggregate analysis conforms with the

limitations in § 3500.17(c)(1). The steps set forth in this section result in maximum limits. Servicers may use accounting procedures that result in lower target balances. In particular, servicers may use a cushion less than the permissible cushion or no cushion at all. This section does not require the use of a cushion.

(2) *Aggregate analysis*. (i) In conducting the escrow account analysis using aggregate analysis, the target balances may not exceed the balances computed according to the following arithmetic operations:

* * * * *

10. Section 3500.21 is amended by revising paragraphs (b) and (c) to read as follows:

§ 3500.21 Mortgage Servicing Transfers.

* * * *

(b) *Servicing Disclosure Statement; Requirements*. (1) At the time an application for a mortgage servicing loan is submitted, or within 3 business days after submission of the application, the lender, mortgage broker who anticipates using table funding, or dealer who anticipates a first lien dealer loan shall provide to each person who applies for such a loan a Servicing Disclosure Statement. A format for the Servicing Disclosure Statement appears as Appendix MS-1 to this part. The specific language of the Servicing Disclosure Statement is not required to be used. The information set forth in "Instructions to Preparer" on the Servicing Disclosure Statement need not be included with the information given to applicants, and material in square brackets is optional or alternative language. The model format may be annotated with additional information

that clarifies or enhances the model language. The lender, table funding mortgage broker, or dealer should use the language that best describes the particular circumstances.

(2) The Servicing Disclosure Statement must indicate whether the servicing of the loan may be assigned, sold, or transferred to any other person at any time while the loan is outstanding. If the lender, table funding mortgage broker, or dealer in a first lien dealer loan will engage in the servicing of the mortgage loan for which the applicant has applied, the disclosure may consist of a statement that the entity will service such loan and does not intend to sell, transfer, or assign the servicing of the loan. If the lender, table funding mortgage broker, or dealer in a first lien dealer loan will not engage in the servicing of the mortgage loan for which the applicant has applied, the disclosure may consist of a statement that such entity intends to assign, sell, or transfer servicing of such mortgage loan before the first payment is due. In all other instances, the disclosure must state that the servicing of the loan may be assigned, sold or transferred while the loan is outstanding.

(c) *Servicing Disclosure Statement; Delivery.* The lender, table funding mortgage broker, or dealer that anticipates a first lien dealer loan shall deliver the Servicing Disclosure Statement within 3 business days from receipt of the application by hand delivery, by placing it in the mail, or, if the applicant agrees, by fax, e-mail, or other electronic means. In the event the borrower is denied credit within the 3 business-day period, no servicing disclosure statement is required to be delivered. If co-applicants indicate the same address on their application, one copy delivered to that address is sufficient. If different addresses are shown by co-applicants on the application, a copy must be delivered to each of the co-applicants.

* * * *

11. A new § 3500.22 is added to read as follows:

§ 3500.22 Severability.

If any particular provision of this part or the application of any particular provision to any person or circumstance is held invalid, the remainder of this part and the application of such provisions to other persons or circumstances shall not be affected by such holding.

12. A new § 3500.23 is added to read as follows:

§ 3500.23 ESIGN applicability.

The Electronic Signatures in Global and National Commerce Act ("ESIGN"), 15 U.S.C. 7001-7031, shall apply to this part.

13. Appendix A to part 3500 is revised in its entirety, including the heading, to read as follows:

APPENDIX A TO PART 3500 – INSTRUCTIONS FOR COMPLETING HUD-1 AND HUD-1A SETTLEMENT STATEMENTS; SAMPLE HUD-1 AND HUD-1A STATEMENTS

The following are instructions for completing the HUD-1 settlement statement, required under section 4 of RESPA and 24 CFR part 3500 (Regulation X) of the Department of Housing and Urban Development regulations. This form is to be used as a statement of actual charges and adjustments paid by the borrower and the seller, to be given to the parties in connection with the settlement. The instructions for completion of the HUD-1 are primarily for the benefit of the settlement agents who prepare the

statements and need not be transmitted to the parties as an integral part of the HUD-1. There is no objection to the use of the HUD-1 in transactions in which its use is not legally required. Refer to the definitions section of HUD's regulations (24 CFR 3500.2) for specific definitions of many of the terms that are used in these instructions.

General Instructions

Information and amounts may be filled in by typewriter, hand printing, computer printing, or any other method producing clear and legible results. Refer to HUD's regulations (Regulation X) regarding rules applicable to reproduction of the HUD-1 for the purpose of including customary recitals and information used locally in settlements; for example, a breakdown of payoff figures, a breakdown of the Borrower's total monthly mortgage payments, check disbursements, a statement indicating receipt of funds, applicable special stipulations between Borrower and Seller, and the date funds are transferred.

The settlement agent shall complete the HUD-1 to itemize all charges imposed upon the Borrower and the Seller by the loan originator and all sales commissions, whether to be paid at settlement or outside of settlement, and any other charges which either the Borrower or the Seller will pay at settlement. Charges for loan origination and title services should not be itemized except as provided in these instructions. For each separately identified settlement service in connection with the transaction, the name of the person ultimately receiving the payment must be shown together with the total amount paid to such person. Items paid to and retained by a loan originator are disclosed as required in the instructions for lines in the 800-series of the HUD-1 (and for per diem interest, in the 900-series of the HUD-1).

As a general rule, charges that are paid for by the seller must be shown in the seller's column on page 2 of the HUD-1 (unless paid outside closing), and charges that are paid for by the borrower must be shown in the borrower's column (unless paid outside closing). However, in order to promote comparability between the charges on the GFE and the charges on the HUD-1, if a seller pays for a charge that was included on the GFE, the charge should be listed in the borrower's column on page 2 of the HUD-1. That charge should also be offset by listing a credit in that amount to the borrower on lines 204-209 on page 1 of the HUD-1, and by a charge to the seller in lines 506-509 on page 1 of the HUD-1. If a loan originator (other than for no-cost loans), real estate agent, other settlement service provider, or other person pays for a charge that was included on the GFE, the charge should be listed in the borrower's column on page 2 of the HUD-1, with an offsetting credit reported on page 1 of the HUD-1, identifying the party paying the charge.

Charges paid outside of settlement by the borrower, seller, loan originator, real estate agent, or any other person, must be included on the HUD-1 but marked "P.O.C." for "Paid Outside of Closing" (settlement) and must not be included in computing totals. However, indirect payments from a lender to a mortgage broker may not be disclosed as P.O.C., and must be included as a credit on Line 802. P.O.C. items must not be placed in the Borrower or Seller columns, but rather on the appropriate line outside the columns. The settlement agent must indicate whether P.O.C. items are paid for by the Borrower, Seller, or some other party by marking the items paid for by whoever made the payment as "P.O.C." with the party making the payment identified in parentheses, such as "P.O.C. (borrower)" or "P.O.C. (seller)".

In the case of "no cost" loans where "no cost" encompasses third party fees as well as the upfront payment to the loan originator, the third party services covered by the "no cost" provisions must be itemized and listed in the borrower's column on the HUD-1/1A with the charge for the third party service. These itemized charges must be offset with a negative adjusted origination charge on Line 803 and recorded in the columns.

Blank lines are provided in section L for any additional settlement charges. Blank lines are also provided for additional insertions in sections J and K. The names of the recipients of the settlement charges in section L and the names of the recipients of adjustments described in section J or K should be included on the blank lines.

Lines and columns in section J which relate to the Borrower's transaction may be left blank on the copy of the HUD–1 which will be furnished to the Seller. Lines and columns in section K which relate to the Seller's transaction may be left blank on the copy of the HUD–1 which will be furnished to the Borrower.

Line Item Instructions

Instructions for completing the individual items on the HUD–1 follow.

Section A. This section requires no entry of information.

Section B. Check appropriate loan type and complete the remaining items as applicable.

Section C. This section provides a notice regarding settlement costs and requires no additional entry of information.

Sections D and E. Fill in the names and current mailing addresses and zip codes of the Borrower and the Seller. Where there is more than one Borrower or Seller, the

name and address of each one is required. Use a supplementary page if needed to list multiple Borrowers or Sellers.

Section F. Fill in the name, current mailing address and zip code of the Lender.

Section G. The street address of the property being sold should be listed. If there is no street address, a brief legal description or other location of the property should be inserted. In all cases give the zip code of the property.

Section H. Fill in name, address, zip code and telephone number of settlement agent, and address and zip code of "place of settlement."

Section I. Fill in date of settlement.

Section J. Summary of Borrower's Transaction. Line 101 is for the contract sales price of the property being sold, excluding the price of any items of tangible personal property if Borrower and Seller have agreed to a separate price for such items.

Line 102 is for the sales price of any items of tangible personal property excluded from Line 101. Personal property could include such items as carpets, drapes, stoves, refrigerators, etc. What constitutes personal property varies from state to state. Manufactured homes are not considered personal property for this purpose.

Line 103 is used to record the total charges to Borrower detailed in Section L and totaled on Line 1400.

Lines 104 and 105 are for additional amounts owed by the Borrower, such as charges that were not listed on the GFE or items paid by the Seller prior to settlement but reimbursed by the Borrower at settlement. For example, the balance in the Seller's reserve account held in connection with an existing loan, if assigned to the Borrower in a loan assumption case, will be entered here. These lines will also be used when a tenant in

the property being sold has not yet paid the rent, which the Borrower will collect, for a period of time prior to the settlement. The lines will also be used to indicate the treatment for any tenant security deposit. The Seller will be credited on Lines 404–405.

Lines 106 through 112 are for items which the Seller had paid in advance, and for which the Borrower must therefore reimburse the Seller. Examples of items for which adjustments will be made may include taxes and assessments paid in advance for an entire year or other period, when settlement occurs prior to the expiration of the year or other period for which they were paid. Additional examples include flood and hazard insurance premiums, if the Borrower is being substituted as an insured under the same policy; mortgage insurance in loan assumption cases; planned unit development or condominium association assessments paid in advance; fuel or other supplies on hand, purchased by the Seller, which the Borrower will use when Borrower takes possession of the property; and ground rent paid in advance.

Line 120 is for the total of Lines 101 through 112.

Line 201 is for any amount paid against the sales price prior to settlement.

Line 202 is for the amount of the new loan made by the Lender when a loan to finance construction of a new structure constructed for sale is used as or converted to a loan to finance purchase. Line 202 should also be used for the amount of the first user loan, when a loan to purchase a manufactured home for resale is converted to a loan to finance purchase by the first user. For other loans covered by 24 CFR part 3500 (Regulation X) which finance construction of a new structure or purchase of a manufactured home, list the sales price of the land on Line 104, the construction cost or purchase price of manufactured home on Line 105 (Line 101 would be left blank in this

instance) and amount of the loan on Line 202. The remainder of the form should be completed taking into account adjustments and charges related to the temporary financing and permanent financing and which are known at the date of settlement.

Line 203 is used for cases in which the Borrower is assuming or taking title subject to an existing loan or lien on the property.

Lines 204–209 are used for other items paid by or on behalf of the Borrower. Lines 204–209 should be used to indicate any financing arrangements or other new loan not listed in Line 202. For example, if the Borrower is using a second mortgage or note to finance part of the purchase price, whether from the same lender, another lender or the Seller, insert the principal amount of the loan with a brief explanation on Lines 204–209. Lines 204-209 should also be used where the Borrower receives a credit from the Seller for closing costs, including seller-paid GFE charges. They may also be used in cases in which a Seller (typically a builder) is making an "allowance" to the Borrower for items that the Borrower is to purchase separately.

Lines 210 through 219 are for items which have not yet been paid, and which the Borrower is expected to pay, but which are attributable in part to a period of time prior to the settlement. In jurisdictions in which taxes are paid late in the tax year, most cases will show the proration of taxes in these lines. Other examples include utilities used but not paid for by the Seller, rent collected in advance by the Seller from a tenant for a period extending beyond the settlement date, and interest on loan assumptions.

Line 220 is for the total of Lines 201 through 219.

Lines 301 and 302 are summary lines for the Borrower. Enter total in Line 120 on Line 301. Enter total in Line 220 on Line 302.

Line 303 must indicate either the cash required from the Borrower at settlement (the usual case in a purchase transaction), or cash payable to the Borrower at settlement (if, for example, the Borrower's earnest money exceeds the Borrower's cash obligations in the transaction or there is a cash-out refinance). Subtract Line 302 from Line 301 and enter the amount of cash due to or from the Borrower at settlement on Line 303. The appropriate box should be checked. If the Borrower's earnest money is applied toward the charge for a settlement service, the amount so applied should not be included on Line 303 but instead should be shown on the appropriate line for the settlement service, marked "P.O.C. (Borrower)", and must not be included in computing totals.

Section K. Summary of Seller's Transaction. Instructions for the use of Lines 101 and 102 and 104–112 above, apply also to Lines 401–412. Line 420 is for the total of Lines 401 through 412.

Line 501 is used if the Seller's real estate broker or other party who is not the settlement agent has received and holds a deposit against the sales price (earnest money) which exceeds the fee or commission owed to that party. If that party will render the excess deposit directly to the Seller, rather than through the settlement agent, the amount of excess deposit should be entered on Line 501 and the amount of the total deposit (including commissions) should be entered on Line 201.

Line 502 is used to record the total charges to the Seller detailed in section L and totaled on Line 1400.

Line 503 is used if the Borrower is assuming or taking title subject to existing liens which are to be deducted from sales price.

Lines 504 and 505 are used for the amounts (including any accrued interest) of any first and/or second loans which will be paid as part of the settlement.

Line 506 is used for deposits paid by the Borrower to the Seller or other party who is not the settlement agent. Enter the amount of the deposit in Line 201 on Line 506 unless Line 501 is used or the party who is not the settlement agent transfers all or part of the deposit to the settlement agent, in which case the settlement agent will note in parentheses on Line 507 the amount of the deposit that is being disbursed as proceeds and enter in the column for Line 506 the amount retained by the above-described party for settlement services. If the settlement agent holds the deposit, insert a note in Line 507 which indicates that the deposit is being disbursed as proceeds.

Lines 506 through 509 may be used to list additional liens which must be paid off through the settlement to clear title to the property. Other Seller obligations should be shown on Lines 506–509, including charges that were disclosed on the GFE but that are actually being paid for by the Seller. These Lines may also be used to indicate funds to be held by the settlement agent for the payment of either repairs, or water, fuel, or other utility bills that cannot be prorated between the parties at settlement because the amounts used by the Seller prior to settlement are not yet known. Subsequent disclosure of the actual amount of these post-settlement items to be paid from settlement funds is optional. Any amounts entered on Lines 204–209 including Seller financing arrangements should also be entered on Lines 506–509.

Instructions for the use of Lines 510 through 519 are the same as those for Lines 210 to 219 above.

Line 520 is for the total of Lines 501 through 519.

Lines 601 and 602 are summary lines for the Seller. Enter the total in Line 420 on Line 610. Enter the total in Line 520 on Line 602.

Line 603 must indicate either the cash required to be paid to the Seller at settlement (the usual case in a purchase transaction), or the cash payable by the Seller at settlement. Subtract Line 602 from Line 601 and enter the amount of cash due to or from the Seller at settlement on Line 603. The appropriate box should be checked.

Section L. Settlement Charges.

Line 700 is used to enter the sales commission charged by the sales agent or real estate broker.

Lines 701–702 are to be used to state the split of the commission where the settlement agent disburses portions of the commission to two or more sales agents or real estate brokers.

Line 703 is used to enter the amount of sales commission disbursed at settlement. If the sales agent or real estate broker is retaining a part of the deposit against the sales price (earnest money) to apply towards the sales agent's or real estate broker's commission, include in Line 703 only that part of the commission being disbursed at settlement and insert a note on Line 704 indicating the amount the sales agent or real estate broker is retaining as a "P.O.C." item.

Line 704 may be used for additional charges made by the sales agent or real estate broker, or for a sales commission charged to the Borrower, which will be disbursed by the settlement agent.

Line 801 is used to record "Our origination charge," which includes all charges received by the loan originator, except any charge for the specific interest rate chosen

(points). This number must not be listed in either the buyer's or seller's column. The amount shown in Line 801 must include any amounts received for origination services, including administrative and processing services, performed by or on behalf of the loan originator.

Line 802 is used to record "Your credit or charge (points) for the specific interest rate chosen," which states the charge or credit adjustment as applied to "Our origination charge," if applicable. This number must not be listed in either column or shown on page one of the HUD-1.

For a mortgage broker originating a loan in its own name, the amount shown on Line 802 will be the difference between the initial loan amount and the total payment to the mortgage broker from the lender. The total payment to the mortgage broker will be the sum of the price paid for the loan by the lender and any other payments to the mortgage broker from the lender, including any payments based on the loan amount or loan terms, and any flat rate payments. For a mortgage broker originating a loan in another entity's name, the amount shown on Line 802 will be the sum of all payments to the mortgage broker from the lender, including any payments based on the loan amount or loan terms, and any flat rate payments.

In either case, when the amount paid to the mortgage broker exceeds the initial loan amount, there is a credit to the borrower and it is entered as a negative amount. When the initial loan amount exceeds the amount paid to the mortgage broker, there is a charge to the borrower and it is entered as a positive amount. For a lender, the amount shown on Line 802 may include any credit or charge (points) to the Borrower.

Line 803 is used to record "Your adjusted origination charges," which states the net amount of the loan origination charges, the sum of the amounts shown in Lines 801 and 802. This amount must be listed in the columns as either a positive number (for example, where the origination charge shown in Line 801 exceeds any credit for the interest rate shown in Line 802 or where there is an origination charge in Line 801 and a charge for the interest rate (points) is shown on Line 802) or as a negative number (for example, where the credit for the interest rate shown in Line 802 exceeds the origination charges shown in Line 801).

In the case of "no cost" loans, where "no cost" refers only to the loan originator's fees, the amounts shown in Lines 801 and 802 should offset, so that the charge shown on Line 803 is zero. Where "no cost" includes third party settlement services, the credit shown in Line 802 will more than offset the amount shown in Line 801. The amount shown in Line 803 will be a negative number to offset the settlement charges paid indirectly through the loan originator.

Lines 804-808 may be used to record each of the "Required services that we select." Each settlement service provider must be identified by name and the amount paid recorded either inside the columns or as paid to the provider outside closing ("P.O.C."), as described in the General Instructions.

Line 804 is used to record the appraisal fee.

Line 805 is used to record the fee for all credit reports.

Line 806 is used to record the fee for any tax service.

Line 807 is used to record any flood certification fee.

Lines 808 and additional sequentially numbered lines, as needed, are used to record other third party services required by the loan originator. These Lines may also be used to record other required disclosures from the loan originator. Any such disclosures must be listed outside the columns.

Lines 901–904. This series is used to record the items which the Lender requires to be paid at the time of settlement, but which are not necessarily paid to the lender (e.g., FHA mortgage insurance premium), other than reserves collected by the Lender and recorded in the 1000-series.

Line 901 is used if interest is collected at settlement for a part of a month or other period between settlement and the date from which interest will be collected with the first regular monthly payment. Enter that amount here and include the per diem charges. If such interest is not collected until the first regular monthly payment, no entry should be made on Line 901.

Line 902 is used for mortgage insurance premiums due and payable at settlement, including any monthly amounts due at settlement and any upfront mortgage insurance premium, but not including any reserves collected by the Lender and recorded in the 1000-series. If a lump sum mortgage insurance premium paid at settlement is included on Line 902, a note should indicate that the premium is for the life of the loan.

Line 903 is used for homeowner's insurance premiums that the Lender requires to be paid at the time of settlement, except reserves collected by the Lender and recorded in the 1000-series.

Lines 904 and additional sequentially numbered lines are used to list additional items required by the Lender (except for reserves collected by the Lender and recorded in

the 1000-series), including premiums for flood or other insurance. These lines are also used to list amounts paid at settlement for insurance not required by the Lender.

Lines 1000-1007. This series is used for amounts collected by the Lender from the Borrower and held in an account for the future payment of the obligations listed as they fall due. Include the time period (number of months) and the monthly assessment. In many jurisdictions this is referred to as an "escrow", "impound", or "trust" account. In addition to the property taxes and insurance listed, some Lenders may require reserves for flood insurance, condominium owners' association assessments, etc. The amount in line 1001 must be listed in the columns, and the itemizations in lines 1002 through 1007 must be listed outside the columns.

After itemizing individual deposits in the 1000 series, the servicer shall make an adjustment based on aggregate accounting. This adjustment equals the difference between the deposit required under aggregate accounting and the sum of the itemized deposits. The computation steps for aggregate accounting are set out in 24 CFR § 3500.17(d). The adjustment will always be a negative number or zero (-0-), except for amounts due to rounding. The settlement agent shall enter the aggregate adjustment amount outside the columns on a final line of the 1000 series of the HUD-1 or HUD-1A statement. Appendix E to this part sets out an example of aggregate analysis.

Lines 1100-1108. This series covers title charges and charges by attorneys and closing or settlement agents. The title charges include a variety of services performed by title companies or others, and include fees directly related to the transfer of title (title examination, title search, document preparation), fees for title insurance, and fees for conducting the closing. The legal charges include fees for attorneys representing the

lender, seller, or borrower, and any attorney preparing title work. The series also includes any settlement, notary, and delivery fees related to the services covered in this series. Disbursements to third parties must be broken out in the appropriate lines or in blank lines in the series, and amounts paid to these third parties must be shown outside of the columns if included in Line 1101. Charges not included in Line 1101 must be listed in the columns.

Line 1101 is used to record the total for the category of "Title services and lender's title insurance." This amount must be listed in the columns.

Line 1102 is used to record the settlement or closing fee.

Line 1103 is used to record the charges for the owner's title insurance and related endorsements. This amount must be listed in the columns.

Line 1104 is used to record the lender's title insurance premium and related endorsements.

Line 1105 is used to record the amount of the lender's title policy limit. This amount is recorded outside of the columns.

Line 1106 is used to record the amount of the owner's title policy limit. This amount is recorded outside of the columns.

Line 1107 is used to record the amount of the total title insurance premium, including endorsements, that is retained by the title agent. This amount is recorded outside of the columns.

Line 1108 used to record the amount of the total title insurance premium, including endorsements, that is retained by the title underwriter. This amount is recorded outside of the columns.

Additional sequentially numbered lines in the 1100-series may be used to itemize title charges paid to other third parties, as identified by name and type of service provided.

Lines 1200-1206. This series covers government recording and transfer charges. Charges paid by the borrower must be listed in the columns as described for lines 1201 and 1203, with itemizations shown outside the columns. Any amounts that are charged to the seller and that were not included on the Good Faith Estimate must be listed in the columns.

Line 1201 is used to record the total "Government recording charges," and the amount must be listed in the columns.

Line 1202 is used to record, outside of the columns, the itemized recording charges.

Line 1203 is used to record the transfer taxes, and the amount must be listed in the columns.

Line 1204 is used to record, outside of the columns, the amounts for local transfer taxes and stamps.

Line 1205 is used to record, outside of the columns, the amounts for State transfer taxes and stamps.

Line 1206 and additional sequentially numbered lines may be used to record specific itemized third party charges for government recording and transfer services, but the amounts must be listed outside the columns.

Line 1301 and additional sequentially numbered lines must be used to record required services that the borrower can shop for, such as fees for survey, pest inspection,

or other similar inspections. These lines may also be used to record additional itemized settlement charges that are not included in a specific category, such as fees for structural and environmental inspections; pre-sale inspections of heating, plumbing or electrical equipment; or insurance or warranty coverage. The amounts must be listed in either the borrower's or seller's column.

Line 1400 must state the total settlement charges as calculated by adding the amounts within each column.

Page 3.

Comparison of Good Faith Estimate (GFE) and HUD-1/1A Charges

The comparison chart must be prepared using the exact information and amounts from the GFE and the actual settlement charges shown on the HUD-1/1A Settlement Statement. The comparison chart is comprised of three sections: "Charges That Cannot Increase", "Charges That Cannot Increase More Than 10%", and "Charges That Can Change".

"Charges That Cannot Increase". The amounts shown in Blocks 1 and 2, in Line A, and in Block 8 on the borrower's GFE must be entered in the appropriate line in the Good Faith Estimate column. The amounts shown on Lines 801, 802, 803 and 1203 of the HUD-1/1A must be entered in the corresponding line in the HUD-1/1A column. The HUD-1/1A column must include any amounts shown on page 2 of the HUD-1 in the column as paid for by the borrower, plus any amounts that are shown as P.O.C. by or on behalf of the borrower. If there is a credit in Block 2 of the GFE or Line 802 of the HUD-1/1A, the credit should be entered as a negative number.

"Charges That Cannot Increase More Than 10%". A description of each charge included in Blocks 3 and 7 on the borrower's GFE must be entered on separate lines in this section, with the amount shown on the borrower's GFE for each charge entered in the corresponding line in the Good Faith Estimate column. For each charge included in Blocks 4, 5 and 6 on the borrower's GFE for which the loan originator selected the provider or for which the borrower selected a provider identified by the loan originator, a description must be entered on a separate line in this section, with the amount shown on the borrower's GFE for each charge entered in the corresponding line in the Good Faith Estimate column. The loan originator must identify any third party settlement services for which the borrower selected a provider other than one identified by the loan originator so that the settlement agent can include those charges in the appropriate category. Additional lines may be added if necessary. The amounts shown on the HUD-1/1A for each line must be entered in the HUD-1/1A column next to the corresponding charge from the GFE, along with the appropriate HUD-1/1A line number. The HUD-1/1A column must include any amounts shown on page 2 of the HUD-1 in the column as paid for by the borrower, plus any amounts that are shown as P.O.C. by or on behalf of the borrower.

The amounts shown in the Good Faith Estimate and HUD-1/1A columns for this section must be separately totaled and entered in the designated line. If the total for the HUD-1/1A column is greater than the total for the Good Faith Estimate column, then the amount of the increase must be entered both as a dollar amount and as a percentage increase in the appropriate line.

"Charges That Can Change". The amounts shown in Blocks 9, 10 and 11 on the borrower's GFE must be entered in the appropriate line in the Good Faith Estimate column. Any third party settlement services for which the borrower selected a provider other than one identified by the loan originator must also be included in this section. The amounts shown on the HUD-1/1A for each charge in this section must be entered in the corresponding line in the HUD-1/1A column, along with the appropriate HUD-1/1A line number. The HUD-1/1A column must include any amounts shown on page 2 of the HUD-1 in the column as paid for by the borrower, plus any amounts that are shown as P.O.C. by or on behalf of the borrower. Additional lines may be added if necessary.

Loan Terms

This section must be completed in accordance with the information and instructions provided by the lender. The lender must provide this information in a format that permits the settlement agent to simply enter the necessary information in the appropriate spaces, without the settlement agent having to refer to the loan documents themselves.

INSTRUCTIONS FOR COMPLETING HUD-1A

Note: The HUD-1A is an optional form that may be used for refinancing and subordinate-lien federally related mortgage loans, as well as for any other one-party transaction that does not involve the transfer of title to residential real property. The HUD-1 form may also be used for such transactions, by utilizing the borrower's side of the HUD-1 and following the relevant parts of the instructions as set forth above. The use of either the HUD-1 or HUD-1A is not mandatory for open-end lines of credit (home-equity plans), as long as the provisions of Regulation Z are followed.

Background

The HUD-1A settlement statement is to be used as a statement of actual charges and adjustments to be given to the borrower at settlement, as defined in this part. The instructions for completion of the HUD-1A are for the benefit of the settlement agent who prepares the statement; the instructions are not a part of the statement and need not be transmitted to the borrower. There is no objection to using the HUD-1A in transactions in which it is not required, and its use in open-end lines of credit transactions (home-equity plans) is encouraged. It may not be used as a substitute for a HUD-1 in any transaction that has a seller.

Refer to the "definitions" section (§ 3500.2) of 24 CFR part 3500 (Regulation X) for specific definitions of terms used in these instructions.

General Instructions

Information and amounts may be filled in by typewriter, hand printing, computer printing, or any other method producing clear and legible results. Refer to 24 CFR § 3500.9 regarding rules for reproduction of the HUD-1A. Additional pages may be attached to the HUD-1A for the inclusion of customary recitals and information used locally for settlements or if there are insufficient lines on the HUD-1A. The settlement agent shall complete the HUD-1A in accordance with the instructions for the HUD-1 to the extent possible, including the instructions for disclosing items paid outside closing and for no cost loans.

Blank lines are provided in Section L for any additional settlement charges. Blank lines are also provided in Section M for recipients of all or portions of the loan proceeds. The names of the recipients of the settlement charges in Section L and the

names of the recipients of the loan proceeds in Section M should be set forth on the blank lines.

Line-Item Instructions

Page 1

The identification information at the top of the HUD-1A should be completed as follows:

The borrower's name and address is entered in the space provided. If the property securing the loan is different from the borrower's address, the address or other location information on the property should be entered in the space provided. The loan number is the lender's identification number for the loan. The settlement date is the date of settlement in accordance with 24 CFR § 3500.2, not the end of any applicable rescission period. The name and address of the lender should be entered in the space provided.

Section L. Settlement Charges. This section of the HUD-1A is similar to Section L of the HUD-1, with minor changes or omissions, including deletion of lines 700 through 704, relating to real estate broker commissions. The instructions for Section L in the HUD-1, should be followed insofar as possible. Inapplicable charges should be ignored, as should any instructions regarding seller items.

Line 1400 in the HUD-1A is for the total settlement charges charged to the borrower. Enter this total on line 1601. This total should include Section L amounts from additional pages, if any are attached to this HUD-1A.

Section M. Disbursement to Others. This section is used to list payees, other than the borrower, of all or portions of the loan proceeds (including the lender, if the loan is paying off a prior loan made by the same lender), when the payee will be paid directly

out of the settlement proceeds. It is not used to list payees of settlement charges, nor to list funds disbursed directly to the borrower, even if the lender knows the borrower's intended use of the funds.

For example, in a refinancing transaction, the loan proceeds are used to pay off an existing loan. The name of the lender for the loan being paid off and the pay-off balance would be entered in Section M. In a home improvement transaction when the proceeds are to be paid to the home improvement contractor, the name of the contractor and the amount paid to the contractor would be entered in Section M. In a consolidation loan, or when part of the loan proceeds is used to pay off other creditors, the name of each creditor and the amount paid to that creditor would be entered in Section M. If the proceeds are to be given directly to the borrower and the borrower will use the proceeds to pay off existing obligations, this would not be reflected in Section M.

Section N. Net Settlement. Line 1600 normally sets forth the principal amount of the loan as it appears on the related note for this loan. In the event this form is used for an open-ended home equity line whose approved amount is greater than the initial amount advanced at settlement, the amount shown on Line 1600 will be the loan amount advanced at settlement. Line 1601 is used for all settlement charges that both are included in the totals for lines 1400 and 1602, and are not financed as part of the principal amount of the loan. This is the amount normally received by the lender from the borrower at settlement, which would occur when some or all of the settlement charges were paid in cash by the borrower at settlement, instead of being financed as part of the principal amount of the loan. Failure to include any such amount in line 1601 will result

in an error in the amount calculated on line 1604. Items paid outside of closing (P.O.C.) should not be included in Line 1601.

Line 1602 is the total amount from line 1400.

Line 1603 is the total amount from line 1520.

Line 1604 is the amount disbursed to the borrower. This is determined by adding together the amounts for lines 1600 and 1601, and then subtracting any amounts listed on lines 1602 and 1603.

Page 2

This section of the HUD-1A is similar to page 3 of the HUD-1. The instructions for page 3 of the HUD-1, should be followed insofar as possible. The HUD-1/1A Column should include any amounts shown on page 1 of the HUD-1A in the column as paid for by the borrower, plus any amounts that are shown as P.O.C. by the borrower. Inapplicable charges should be ignored.

OMB Approval No. 2502-0265

A. Settlement Statement (HUD-1)

B. Type of Loan			
1. ☐ FHA 2. ☐ RHS 3. ☐ Conv. Unins. 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. Property Location:	H. Settlement Agent:	I. Settlement Date:
	Place of Settlement:	

J. Summary of Borrower's Transaction			K. Summary of Seller's Transaction		
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 unpaid 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 220)		( )	602. Less reductions in amount due seller (line 520)		( )
303. Cash ☐ **From** ☐ **To Borrower**			**603. Cash** ☐ **To** ☐ **From Seller**		

The Public Reporting Burden for this collection of information is estimated at 35 minutes per response for collecting, reviewing, and reporting the data. This agency may not collect this information, and you are not required to complete this form, unless it displays a currently valid OMB control number. No confidentiality is assured; this disclosure is mandatory. This is designed to provide the parties to a RESPA covered transaction with information during the settlement process.

L. Settlement Charges

700. Total Real Estate Broker Fees	Paid From Borrower's Funds at Settlement	Paid From Seller's Funds at Settlement
Division of commission (line 700) as follows:		
701. $ to		
702. $ to		
703. Commission paid at settlement		
704.		

800. Items Payable in Connection with Loan			
801. Our origination charge $ (from GFE #1)			
802. Your credit or charge (points) for the specific interest rate chosen $ (from GFE #2)			
803. Your adjusted origination charges (from GFE A)			
804. Appraisal fee to (from GFE #3)			
805. Credit report to (from GFE #3)			
806. Tax service to (from GFE #3)			
807. Flood certification (from GFE #3)			
808.			

900. Items Required by Lender to Be Paid in Advance		
901. Daily interest charges from to @ $ /day (from GFE #10)		
902. Mortgage insurance premium for months to (from GFE #3)		
903. Homeowner's insurance for years to (from GFE #11)		
904.		

1000. Reserves Deposited with Lender		
1001. Initial deposit for your escrow account (from GFE #9)		
1002. Homeowner's insurance months @ $ per month $		
1003. Mortgage insurance months @ $ per month $		
1004. Property taxes months @ $ per month $		
1005. months @ $ per month $		
1006. months @ $ per month $		
1007. Aggregate Adjustment –$		

1100. Title Charges		
1101. Title services and lender's title insurance (from GFE #4)		
1102. Settlement or closing fee $		
1103. Owner's title insurance (from GFE #5)		
1104. Lender's title insurance $		
1105. Lender's title policy limit $		
1106. Owner's title policy limit $		
1107. Agent's portion of the total title insurance premium $		
1108. Underwriter's portion of the total title insurance premium $		

1200. Government Recording and Transfer Charges		
1201. Government recording charges (from GFE #7)		
1202. Deed $ Mortgage $ Releases $		
1203. Transfer taxes (from GFE #8)		
1204. City/County tax/stamps Deed $ Mortgage $		
1205. State tax/stamps Deed $ Mortgage $		
1206.		

1300. Additional Settlement Charges		
1301. Required services that you can shop for (from GFE #6)		
1302. $		
1303. $		
1304.		
1305.		

1400. Total Settlement Charges (enter on lines 103, Section J and 502, Section K)		

Comparison of Good Faith Estimate (GFE) and HUD-1 Charges		Good Faith Estimate	HUD-1
Charges That Cannot Increase	**HUD-1 Line Number**		
Our origination charge	# 801		
Your credit or charge (points) for the specific interest rate chosen	# 802		
Your adjusted origination charges	# 803		
Transfer taxes	#1203		

Charges That in Total Cannot Increase More Than 10%		Good Faith Estimate	HUD-1
Government recording charges	# 1201		
	#		
	#		
	#		
	#		
	#		
	#		
	#		
	Total		
	Increase between GFE and HUD-1 Charges	**$**	**or** **%**

Charges That Can Change		Good Faith Estimate	HUD-1
Initial deposit for your escrow account	#1001		
Daily interest charges	# 901 $ /day		
Homeowner's insurance	# 903		
	#		
	#		
	#		

Loan Terms

Your initial loan amount is	$
Your loan term is	years
Your initial interest rate is	%
Your initial monthly amount owed for principal, interest, and and any mortgage insurance is	$ includes ☐ Principal ☐ Interest ☐ Mortgage Insurance
Can your interest rate rise?	☐ No. ☐ Yes, it can rise to a maximum of %. The first change will be on and can change again every after . Every change date, your interest rate can increase or decrease by %. Over the life of the loan, your interest rate is guaranteed to never be **lower** than % or **higher** than %.
Even if you make payments on time, can your loan balance rise?	☐ No. ☐ Yes, it can rise to a maximum of $.
Even if you make payments on time, can your monthly amount owed for principal, interest, and mortgage insurance rise?	☐ No. ☐ Yes, the first increase can be on and the monthly amount owed can rise to $. The maximum it can ever rise to is $.
Does your loan have a prepayment penalty?	☐ No. ☐ Yes, your maximum prepayment penalty is $.
Does your loan have a balloon payment?	☐ No. ☐ Yes, you have a balloon payment of $ due in years on .
Total monthly amount owed including escrow account payments	☐ You do not have a monthly escrow payment for items, such as property taxes and homeowner's insurance. You must pay these items directly yourself. ☐ You have an additional monthly escrow payment of $ that results in a total initial monthly amount owed of $. This includes principal, interest, any mortgage insurance and any items checked below: ☐ Property taxes ☐ Homeowner's insurance ☐ Flood insurance ☐ ☐ ☐

Note: If you have any questions about the Settlement Charges and Loan Terms listed on this form, please contact your lender.

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Settlement Statement (HUD-1A)

Optional Form for Transactions without Sellers

Name and Address of Borrower:	Name and Address of Lender:
Property Location: (if different from above)	Settlement Agent:
	Place of Settlement:
Loan Number:	Settlement Date:

L. Settlement Charges			
800. Items Payable in Connection with Loan			
801. Our origination charge		(from GFE #1) $	
802. Your credit or charge (points) for the specific interest rate chosen		(from GFE #2) $	
803. Your adjusted origination charges		(from GFE A)	
804. Appraisal fee to		(from GFE #3)	
805. Credit report to		(from GFE #3)	
806. Tax service to		(from GFE #3)	
807. Flood certification		(from GFE #3)	
808.			
900. Items Required by Lender to Be Paid in Advance			
901. Daily interest charges from	to	@ $ /day (from GFE #10)	
902. Mortgage insurance premium	for	months to (from GFE #3)	
903. Homeowner's insurance	for	years to (from GFE #11)	
904.			
1000. Reserves Deposited with Lender			
1001. Initial deposit for your escrow account		(from GFE #9)	
1002. Homeowner's insurance	months @ $	per month $	
1003. Mortgage insurance	months @ $	per month $	
1004. Property taxes	months @ $	per month $	
1005.	months @ $	per month $	
1006.	months @ $	per month $	
1007. Aggregate Adjustment		–$	
1100. Title Charges			
1101. Title services and lender's title insurance		(from GFE #4)	
1102. Settlement or closing fee		$	
1103. Owner's title insurance		(from GFE #5)	
1104. Lender's title insurance		$	
1105. Lender's title policy limit $			
1106. Owner's title policy limit $			
1107. Agent's portion of the total title insurance premium		$	
1108. Underwriter's portion of the total title insurance premium		$	
1200. Government Recording and Transfer Charges			
1201. Government recording charges		(from GFE #7)	
1202. Deed $	Mortgage $	Releases $	
1203. Transfer taxes		(from GFE #8)	
1204. City/County tax/stamps	Deed $	Mortgage $	
1205. State tax/stamps	Deed $	Mortgage $	
1206.			
1300. Additional Settlement Charges			
1301. Required services that you can shop for		(from GFE #6)	
1302.		$	
1303.		$	
1304.			
1305.			
1400. Total Settlement Charges (enter on line 1602, Section N)			

M. Disbursements to Others	
1501.	
1502.	
1503.	
1504.	
1505.	
1506.	
1507.	
1508.	
1509	
1510.	
1511.	
1512.	
1513.	
1514.	
1515.	
1520. Total Disbursed (enter on line 1603)	

N. Net Settlement	
1600. Loan Amount	$
1601. **Plus** Cash/Check from Borrower	$
1602. **Minus** Total Settlement Charges (line 1400)	$
1603. **Minus** Total Disbursements to Others (line 1520)	$
1604. **Equals** Total Disbursements to Borrower (after expiration of any applicable rescission period required by law)	**$**

The Public Reporting Burden for this collection of information is estimated at 35 minutes per response for collecting, reviewing, and reporting the data. This agency may not collect this information, and you are not required to complete this form, unless it displays a currently valid OMB control number. No confidentiality is assured; this disclosure is mandatory. This is designed to provide the parties to a RESPA covered transaction with information during the settlement process.

Comparison of Good Faith Estimate (GFE) and HUD-1A Charges		Good Faith Estimate	HUD-1A
Charges That Cannot Increase	**HUD-1A Line Number**		
Our origination charge	# 801		
Your credit or charge (points) for the specific interest rate chosen	# 802		
Your adjusted origination charges	# 803		
Transfer taxes	#1203		

Charges That in Total Cannot Increase More Than 10%		Good Faith Estimate	HUD-1A
Government recording charges	# 1201		
	#		
	#		
	#		
	#		
	#		
	#		
	#		
Total			
Increase between GFE and HUD-1A Charges		**$ or %**	

Charges That Can Change		Good Faith Estimate	HUD-1A
Initial deposit for your escrow account	#1001		
Daily interest charges	# 901 $ /day		
Homeowner's insurance	# 903		
	#		
	#		
	#		

Loan Terms

Your initial loan amount is	$
Your loan term is	years
Your initial interest rate is	%
Your initial monthly amount owed for principal, interest, and and any mortgage insurance is	$ includes ☐ Principal ☐ Interest ☐ Mortgage Insurance
Can your interest rate rise?	☐ No. ☐ Yes, it can rise to a maximum of %. The first change will be on and can change again every after . Every change date, your interest rate can increase or decrease by %. Over the life of the loan, your interest rate is guaranteed to never be **lower** than % or **higher** than %.
Even if you make payments on time, can your loan balance rise?	☐ No. ☐ Yes, it can rise to a maximum of $.
Even if you make payments on time, can your monthly amount owed for principal, interest, and mortgage insurance rise?	☐ No. ☐ Yes, the first increase can be on and the monthly amount owed can rise to $. The maximum it can ever rise to is $.
Does your loan have a prepayment penalty?	☐ No. ☐ Yes, your maximum prepayment penalty is $.
Does your loan have a balloon payment?	☐ No. ☐ Yes, you have a balloon payment of $ due in years on .
Total monthly amount owed including escrow account payments	☐ You do not have a monthly escrow payment for items, such as property taxes and homeowner's insurance. You must pay these items directly yourself. ☐ You have an additional monthly escrow payment of $ that results in a total initial monthly amount owed of $. This includes principal, interest, any mortgage insurance and any items checked below: ☐ Property taxes ☐ Homeowner's insurance ☐ Flood insurance ☐ ☐ ☐

Note: If you have any questions about the Settlement Charges and Loan Terms listed on this form, please contact your lender.

14. Appendix C to part 3500 is revised in its entirety, including the heading, to read as follows:

APPENDIX C TO PART 3500 – INSTRUCTIONS FOR COMPLETING GOOD FAITH ESTIMATE (GFE) FORM

The following are instructions for completing the GFE required under section 5 of RESPA and 24 CFR 3500.7 of the Department of Housing and Urban Development regulations. The standardized form set forth in this Appendix is the required GFE form and must be provided exactly as specified. The instructions for completion of the GFE are primarily for the benefit of the loan originator who prepares the form and need not be transmitted to the borrower(s) as an integral part of the GFE. The required standardized GFE form must be prepared completely and accurately. A separate GFE must be provided for each loan where a transaction will involve more than one mortgage loan.

General instructions

The loan originator preparing the GFE may fill in information and amounts on the form by typewriter, hand printing, computer printing, or any other method producing clear and legible results. Under these instructions, the "form" refers to the required standardized GFE form. Although the standardized GFE is a prescribed form, Blocks 3, 6, and 11 on page 2 may be adapted for use in particular loan situations, so that additional lines may be inserted there, and unused lines may be deleted.

All fees for categories of charges shall be disclosed in U.S. dollar and cent amounts.

Specific instructions

Page 1.

Top of the Form – The loan originator must enter its name, business address, telephone number, and email address, if any, on the top of the form, along with the applicant's name, the address or location of the property for which financing is sought, and the date of the GFE.

"Purpose." – This section describes the general purpose of the GFE as well as additional information available to the applicant.

"Shopping for your loan." – This section requires no loan originator action.

"Important dates." – This section briefly states important deadlines after which the loan terms that are the subject of the GFE may not be available to the applicant. In Line 1, the loan originator must state the date and, if necessary, time until which the interest rate for the GFE will be available. In Line 2, the loan originator must state the date until which the estimate of all other settlement charges for the GFE will be available. This date must be at least 10 business days from the date of the GFE. In Line 3, the loan originator must state how many calendar days within which the applicant must go to settlement once the interest rate is locked. In Line 4, the loan originator must state how many calendar days prior to settlement the interest rate would have to be locked, if applicable.

"Summary of your loan." – In this section, for all loans the loan originator must fill in, where indicated:

(i) The initial loan amount;

(ii) The loan term; and

(iii) The initial interest rate.

The loan originator must fill in the initial monthly amount owed for principal, interest, and any mortgage insurance. The amount shown must be the greater of: (1) the required monthly payment for principal and interest for the first regularly scheduled payment, plus any monthly mortgage insurance payment; or (2) the accrued interest for the first regularly scheduled payment, plus any monthly mortgage insurance payment.

The loan originator must indicate whether the interest rate can rise, and, if it can, must insert the maximum rate to which it can rise over the life of the loan. The loan originator must also indicate the period of time after which the interest rate can first change.

The loan originator must indicate whether the loan balance can rise even if the borrower makes payments on time, for example in the case of a loan with negative amortization. If it can, the loan originator must insert the maximum amount to which the loan balance can rise over the life of the loan. For federal, state, local, or tribal housing programs that provide payment assistance, any repayment of such program assistance should be excluded from consideration in completing this item. If the loan balance will increase only because escrow items are being paid through the loan balance, the loan originator is not required to check the box indicating that the loan balance can rise.

The loan originator must indicate whether the monthly amount owed for principal, interest, and any mortgage insurance can rise even if the borrower makes payments on time. If the monthly amount owed can rise even if the borrower makes payments on time, the loan originator must indicate the period of time after which the monthly amount owed can first change, the maximum amount to which the monthly amount owed can rise at the time of the first change, and the maximum amount to which the monthly amount

owed can rise over the life of the loan. The amount used for the monthly amount owed must be the greater of: (1) the required monthly payment for principal and interest for that month, plus any monthly mortgage insurance payment; or (2) the accrued interest for that month, plus any monthly mortgage insurance payment.

The loan originator must indicate whether the loan includes a prepayment penalty, and, if so, the maximum amount that it could be.

The loan originator must indicate whether the loan requires a balloon payment and, if so, the amount of the payment and in how many years it will be due.

"Escrow account information." – The loan originator must indicate whether the loan includes an escrow account for property taxes and other financial obligations. The amount shown in the "Summary of your loan" section for "Your initial monthly amount owed for principal, interest, and any mortgage insurance" must be entered in the space for the monthly amount owed in this section.

"Summary of your settlement charges." – On this line, the loan originator must state the Adjusted Origination Charges from subtotal A of page 2, the Charges for All Other Settlement Services from subtotal B of page 2, and the Total Estimated Settlement Charges from the bottom of page 2.

Page 2.

"Understanding your estimated settlement charges." – This section details 11 settlement cost categories and amounts associated with the mortgage loan. For purposes of determining whether a tolerance has been met, the amount on the GFE should be compared with the total of any amounts shown on the HUD-1 in the borrower's column and any amounts paid outside closing by or on behalf of the borrower.

"Your Adjusted Origination Charges"

Block 1, "Our origination charge." – The loan originator must state here all charges that all loan originators involved in this transaction will receive, except for any charge for the specific interest rate chosen (points). A loan originator may not separately charge any additional fees for getting this loan, including for application, processing, or underwriting. The amount stated in Block 1 is subject to zero tolerance, i.e., the amount may not increase at settlement.

Block 2, "Your credit or charge (points) for the specific interest rate chosen." – For transactions involving mortgage brokers, the mortgage broker must indicate through check boxes whether there is a credit to the borrower for the interest rate chosen on the loan, the interest rate, and the amount of the credit, or whether there is an additional charge (points) to the borrower for the interest rate chosen on the loan, the interest rate, and the amount of that charge. **Only one of the boxes may be checked; a credit and charge cannot occur together in the same transaction.**

For transactions without a mortgage broker, the lender may choose not to separately disclose in this block any credit or charge for the interest rate chosen on the loan; however, if this block does not include any positive or negative figure, the lender must check the first box to indicate that "The credit or charge for the interest rate you have chosen" is included in "Our origination charge" above (see Block 1 instructions above), must insert the interest rate, and must also insert "0" in Block 2. **Only one of the boxes may be checked; a credit and charge cannot occur together in the same transaction.**

For a mortgage broker, the credit or charge for the specific interest rate chosen is the net payment to the mortgage broker from the lender (i.e., the sum of all payments to the mortgage broker from the lender, including payments based on the loan amount, a flat rate, or any other computation, and in a table funded transaction, the loan amount less the price paid for the loan by the lender). When the net payment to the mortgage broker from the lender is positive, there is a credit to the borrower and it is entered as a negative amount in Block 2 of the GFE. When the net payment to the mortgage broker from the lender is negative, there is a charge to the borrower and it is entered as a positive amount in Block 2 of the GFE. If there is no net payment (i.e., the credit or charge for the specific interest rate chosen is zero), the mortgage broker must insert "0" in Block 2 and may check either the box indicating there is a credit of "0" or the box indicating there is a charge of "0".

The amount stated in Block 2 is subject to zero tolerance while the interest rate is locked, i.e., any credit for the interest rate chosen cannot decrease in absolute value terms and any charge for the interest rate chosen cannot increase. (Note: An increase in the credit is allowed since this increase is a reduction in cost to the borrower. A decrease in the credit is not allowed since it is an increase in cost to the borrower.)

Line A, "Your Adjusted Origination Charges." – The loan originator must add the numbers in Blocks 1 and 2 and enter this subtotal at highlighted Line A. The subtotal at Line A will be a negative number if there is a credit in Block 2 that exceeds the charge in Block 1. The amount stated in Line A is subject to zero tolerance while the interest rate is locked.

In the case of "no cost" loans, where "no cost" refers only to the loan originator's fees, Line A must show a zero charge as the adjusted origination charge. In the case of "no cost" loans where "no cost" encompasses third party fees as well as the upfront payment to the loan originator, all of the third party fees listed in Block 3 through Block 11 to be paid for by the loan originator (or borrower, if any) must be itemized and listed on the GFE. The credit for the interest rate chosen must be large enough that the total for Line A will result in a negative number to cover the third party fees.

"Your Charges for All Other Settlement Services"

There is a 10 percent tolerance applied to the sum of the prices of each service listed in Block 3, Block 4, Block 5, Block 6, and Block 7, where the loan originator requires the use of a particular provider or the borrower uses a provider selected or identified by the loan originator. Any services in Block 4, Block 5, or Block 6 for which the borrower selects a provider other than one identified by the loan originator are not subject to any tolerance and, at settlement, would not be included in the sum of the charges on which the 10 percent tolerance is based. Where a loan originator permits a borrower to shop for third party settlement services, the loan originator must provide the borrower with a written list of settlement services providers at the time of the GFE, on a separate sheet of paper.

Block 3, "Required services that we select." – In this block, the loan originator must identify each third party settlement service required and selected by the loan originator (excluding title services), along with the estimated price to be paid to the provider of each service. Examples of such third party settlement services might include provision of credit reports, appraisals, flood checks, tax services, and any upfront

mortgage insurance premium. The loan originator must identify the specific required services and provide an estimate of the price of each service. Loan originators are also required to add the individual charges disclosed in this block and place that total in the column of this block. The charge shown in this block is subject to an overall 10 percent tolerance as described above.

Block 4, "Title services and lender's title insurance." – In this block, the loan originator must state the estimated total charge for third party settlement service providers for all closing services, regardless of whether the providers are selected or paid for by the borrower, seller, or loan originator. The loan originator must also include any lender's title insurance premiums, when required, regardless of whether the provider is selected or paid for by the borrower, seller, or loan originator. All fees for title searches, examinations, and endorsements, for example, would be included in this total. The charge shown in this block is subject to an overall 10 percent tolerance as described above.

Block 5, "Owner's title insurance." – In this block, for all purchase transactions the loan originator must provide an estimate of the charge for the owner's title insurance and related endorsements, regardless of whether the providers are selected or paid for by the borrower, seller, or loan originator. For non-purchase transactions, the loan originator may enter "NA" or "Not Applicable" in this Block. The charge shown in this block is subject to an overall 10 percent tolerance as described above.

Block 6, "Required services that you can shop for." – In this block, the loan originator must identify each third party settlement service required by the loan originator where the borrower is permitted to shop for and select the settlement service provider

(excluding title services), along with the estimated charge to be paid to the provider of each service. The loan originator must identify the specific required services (e.g., survey, pest inspection) and provide an estimate of the charge of each service. The loan originator must also add the individual charges disclosed in this block and place the total in the column of this block. The charge shown in this block is subject to an overall 10 percent tolerance as described above.

Block 7, "Government recording charges." – In this block, the loan originator must estimate the state and local government fees for recording the loan and title documents that can be expected to be charged at settlement. The charge shown in this block is subject to an overall 10 percent tolerance as described above.

Block 8, "Transfer taxes." – In this block, the loan originator must estimate the sum of all state and local government fees on mortgages and home sales that can be expected to be charged at settlement, based upon the proposed loan amount or sales price and on the property address. A zero tolerance applies to the sum of these estimated fees.

Block 9, "Initial deposit for your escrow account." – In this block, the loan originator must estimate the amount that it will require the borrower to place into a reserve or escrow account at settlement to be applied to recurring charges for property taxes, homeowner's and other similar insurance, mortgage insurance, and other periodic charges. The loan originator must indicate through check boxes if the reserve or escrow account will cover future payments for all tax, all hazard insurance, and other obligations that the loan originator requires to be paid as they fall due. If the reserve or escrow account includes some, but not all, property taxes or hazard insurance, or if it includes

mortgage insurance, the loan originator should check "other" and then list the items included.

Block 10, "Daily interest charges." – In this block, the loan originator must estimate the total amount that will be due at settlement for the daily interest on the loan from the date of settlement until the first day of the first period covered by scheduled mortgage payments. The loan originator must also indicate how this total amount is calculated by providing the amount of the interest charges per day and the number of days used in the calculation, based on a stated projected closing date.

Block 11, "Homeowner's insurance." – The loan originator must estimate in this block the total amount of the premiums for any hazard insurance policy and other similar insurance, such as fire or flood insurance that must be purchased at or before settlement to meet the loan originator's requirements. The loan originator must also separately indicate the nature of each type of insurance required along with the charges. To the extent a loan originator requires that such insurance be part of an escrow account, the amount of the initial escrow deposit must be included in Block 9.

Line B, "Your Charges for All Other Settlement Services." – The loan originator must add the numbers in Blocks 3 through 11 and enter this subtotal in the column at highlighted Line B.

Line A + B, "Total Estimated Settlement Charges." – The loan originator must add the subtotals in the right-hand column at highlighted Lines A and B and enter this total in the column at highlighted Line A+B.

Page 3.

"Instructions"

"Understanding which charges can change at settlement." – This section informs the applicant about which categories of settlement charges can increase at closing, and by how much, and which categories of settlement charges cannot increase at closing. This section requires no loan originator action.

"Using the tradeoff table." – This section is designed to make borrowers aware of the relationship between their total estimated settlement charges on one hand, and the interest rate and resulting monthly payment on the other hand. The loan originator must complete the left hand column using the loan amount, interest rate, monthly payment figure, and the total estimated settlement charges from page 1 of the GFE. The loan originator, at its option, may provide the borrower with the same information for two alternative loans, one with a higher interest rate, if available, and one with a lower interest rate, if available, from the loan originator. The loan originator should list in the tradeoff table only alternative loans for which it would presently issue a GFE based on the same information the loan originator considered in issuing this GFE. The alternative loans must use the same loan amount and be otherwise identical to the loan in the GFE. The alternative loans must have, for example, the identical number of payment periods; the same margin, index, and adjustment schedule if the loans are adjustable rate mortgages; and the same requirements for prepayment penalty and balloon payments. If the loan originator fills in the tradeoff table, the loan originator must show the borrower the loan amount, alternative interest rate, alternative monthly payment, the change in the monthly payment from the loan in this GFE to the alternative loan, the change in the total settlement charges from the loan in this GFE to the alternative loan, and the total

settlement charges for the alternative loan. If these options are available, an applicant may request a new GFE, and a new GFE must be provided by the loan originator.

"Using the shopping chart." – This chart is a shopping tool to be provided by the loan originator for the borrower to complete, in order to compare GFEs.

"If your loan is sold in the future." – This section requires no loan originator action.

OMB Approval No. 2502-0265

Good Faith Estimate (GFE)

Name of Originator	Borrower
Originator Address	Property Address
Originator Phone Number	
Originator Email	Date of GFE

Purpose

This GFE gives you an estimate of your settlement charges and loan terms if you are approved for this loan. For more information, see HUD's *Special Information Booklet* on settlement charges, your *Truth-in-Lending Disclosures,* and other consumer information at www.hud.gov/respa. If you decide you would like to proceed with this loan, contact us.

Shopping for your loan

Only you can shop for the best loan for you. Compare this GFE with other loan offers, so you can find the best loan. Use the shopping chart on page 3 to compare all the offers you receive.

Important dates

1. The interest rate for this GFE is available through _____. After this time, the interest rate, some of your loan Origination Charges, and the monthly payment shown below can change until you lock your interest rate.
2. This estimate for all other settlement charges is available through _____.
3. After you lock your interest rate, you must go to settlement within ___ days (your rate lock period) to receive the locked interest rate.
4. You must lock the interest rate at least ___ days before settlement.

Summary of your loan

Your initial loan amount is	$	
Your loan term is	years	
Your initial interest rate is	%	
Your initial monthly amount owed for principal, interest, and any mortgage insurance is	$ per month	
Can your interest rate rise?	☐ No	☐ Yes, it can rise to a maximum of %. The first change will be in .
Even if you make payments on time, can your loan balance rise?	☐ No	☐ Yes, it can rise to a maximum of $
Even if you make payments on time, can your monthly amount owed for principal, interest, and any mortgage insurance rise?	☐ No	☐ Yes, the first increase can be in and the monthly amount owed can rise to $. The maximum it can ever rise to is $.
Does your loan have a prepayment penalty?	☐ No	☐ Yes, your maximum prepayment penalty is $.
Does your loan have a balloon payment?	☐ No	☐ Yes, you have a balloon payment of $ due in years.

Escrow account information

Some lenders require an escrow account to hold funds for paying property taxes or other property-related charges in addition to your monthly amount owed of $ _____ .

Do we require you to have an escrow account for your loan?

☐ No, you do not have an escrow account. You must pay these charges directly when due.

☐ Yes, you have an escrow account. It may or may not cover all of these charges. Ask us.

Summary of your settlement charges

A	Your Adjusted Origination Charges *(See page 2.)*	$
B	Your Charges for All Other Settlement Services *(See page 2.)*	$
A + B	Total Estimated Settlement Charges	$

Understanding your estimated settlement charges

Your Adjusted Origination Charges

1. **Our origination charge** This charge is for getting this loan for you.	
2. **Your credit or charge (points) for the specific interest rate chosen** ☐ The credit or charge for the interest rate of ____ % is included in "Our origination charge." (See item 1 above.) ☐ You receive a credit of $ ____ for this interest rate of ____ %. This credit **reduces** your settlement charges. ☐ You pay a charge of $ ____ for this interest rate of ____ %. This charge (points) **increases** your total settlement charges. The tradeoff table on page 3 shows that you can change your total settlement charges by choosing a different interest rate for this loan.	
A Your Adjusted Origination Charges	$

Your Charges for All Other Settlement Services

Some of these charges can change at settlement. See the top of page 3 for more information.

3. **Required services that we select** These charges are for services we require to complete your settlement. We will choose the providers of these services. *Service* — *Charge*	
4. **Title services and lender's title insurance** This charge includes the services of a title or settlement agent, for example, and title insurance to protect the lender, if required.	
5. **Owner's title insurance** You may purchase an owner's title insurance policy to protect your interest in the property.	
6. **Required services that you can shop for** These charges are for other services that are required to complete your settlement. We can identify providers of these services or you can shop for them yourself. Our estimates for providing these services are below. *Service* — *Charge*	
7. **Government recording charges** These charges are for state and local fees to record your loan and title documents.	
8. **Transfer taxes** These charges are for state and local fees on mortgages and home sales.	
9. **Initial deposit for your escrow account** This charge is held in an escrow account to pay future recurring charges on your property and includes ☐ all property taxes, ☐ all insurance, and ☐ other ____.	
10. **Daily interest charges** This charge is for the daily interest on your loan from the day of your settlement until the first day of the next month or the first day of your normal mortgage payment cycle. This amount is $____ per day for ____ days (if your settlement is ____).	
11. **Homeowner's insurance** This charge is for the insurance you must buy for the property to protect from a loss, such as fire. *Policy* — *Charge*	
B Your Charges for All Other Settlement Services	$
A + B Total Estimated Settlement Charges	$

Instructions

Understanding which charges can change at settlement

This GFE estimates your settlement charges. At your settlement, you will receive a HUD-1, a form that lists your actual costs. Compare the charges on the HUD-1 with the charges on this GFE. Charges can change if you select your own provider and do not use the companies we identify. (See below for details.)

These charges **cannot increase** at settlement:	The total of these charges **can increase up to 10%** at settlement:	These charges **can change** at settlement:
▪ Our origination charge ▪ Your credit or charge (points) for the specific interest rate chosen *(after you lock in your interest rate)* ▪ Your adjusted origination charges *(after you lock in your interest rate)* ▪ Transfer taxes	▪ Required services that we select ▪ Title services and lender's title insurance *(if we select them or you use companies we identify)* ▪ Owner's title insurance *(if you use companies we identify)* ▪ Required services that you can shop for *(if you use companies we identify)* ▪ Government recording charges	▪ Required services that you can shop for *(if you do not use companies we identify)* ▪ Title services and lender's title insurance *(if you do not use companies we identify)* ▪ Owner's title insurance *(if you do not use companies we identify)* ▪ Initial deposit for your escrow account ▪ Daily interest charges ▪ Homeowner's insurance

Using the tradeoff table

In this GFE, we offered you this loan with a particular interest rate and estimated settlement charges. However:

- If you want to choose this same loan with **lower settlement charges,** then you will have a **higher interest rate.**
- If you want to choose this same loan with a **lower interest rate,** then you will have **higher settlement charges.**

If you would like to choose an available option, you must ask us for a new GFE.

Loan originators have the option to complete this table. Please ask for additional information if the table is not completed.

	The loan in this GFE	The same loan with lower settlement charges	The same loan with a lower interest rate
Your initial loan amount	$	$	$
Your initial interest rate[1]	%	%	%
Your initial monthly amount owed	$	$	$
Change in the monthly amount owed from this GFE	No change	You will pay $ **more** every month	You will pay $ **less** every month
Change in the amount you will pay at settlement with this interest rate	No change	Your settlement charges will be **reduced** by $	Your settlement charges will **increase** by $
How much your total estimated settlement charges will be	$	$	$

[1] *For an adjustable rate loan, the comparisons above are for the initial interest rate before adjustments are made.*

Using the shopping chart

Use this chart to compare GFEs from different loan originators. Fill in the information by using a different column for each GFE you receive. By comparing loan offers, you can shop for the best loan.

	This loan	Loan 2	Loan 3	Loan 4
Loan originator name				
Initial loan amount				
Loan term				
Initial interest rate				
Initial monthly amount owed				
Rate lock period				
Can interest rate rise?				
Can loan balance rise?				
Can monthly amount owed rise?				
Prepayment penalty?				
Balloon payment?				
Total Estimated Settlement Charges				

If your loan is sold in the future

Some lenders may sell your loan after settlement. Any fees lenders receive in the future cannot change the loan you receive or the charges you paid at settlement.

15. Appendix E to part 3500 is amended by removing the parenthetical "(Existing Accounts)" from the heading, "II. Example Illustrating Single-Item Analysis (Existing Accounts)".

16. Appendix MS-1 to part 3500 is revised to read as follows:

APPENDIX MS-1 TO PART 3500

[Sample language; use business stationery or similar heading]

[Date]

SERVICING DISCLOSURE STATEMENT

NOTICE TO FIRST LIEN MORTGAGE LOAN APPLICANTS: THE RIGHT TO COLLECT YOUR MORTGAGE LOAN PAYMENTS MAY BE TRANSFERRED.

You are applying for a mortgage loan covered by the Real Estate Settlement Procedures Act (RESPA) (12 U.S.C. 2601 et seq.). RESPA gives you certain rights under Federal law. This statement describes whether the servicing for this loan may be transferred to a different loan servicer. "Servicing" refers to collecting your principal, interest, and escrow payments, if any, as well as sending any monthly or annual statements, tracking account balances, and handling other aspects of your loan. You will be given advance notice before a transfer occurs.

Servicing Transfer Information

[We may assign, sell, or transfer the servicing of your loan while the loan is outstanding.]

[or]

[We do not service mortgage loans of the type for which you applied. We intend to assign, sell, or transfer the servicing of your mortgage loan before the first payment is due.]

[or]

[The loan for which you have applied will be serviced at this financial institution and we do not intend to sell, transfer, or assign the servicing of the loan.]

[INSTRUCTIONS TO PREPARER: Insert the date and select the appropriate language under "Servicing Transfer Information." The model format may be annotated with further information that clarifies or enhances the model language.]

DATE: _November 7, 2008____

_____//_____
Brian D. Montgomery, Assistant Secretary for
Housing—Federal Housing Commissioner

[FR-5180-F-03]

Note: The following appendix will not appear in the Code of Federal Regulations.

Appendix to FR- 5180 Final Rule on Regulatory Flexibility Analysis

The following Regulatory Flexibility Analysis is Chapter 6 of the final rule's Economic Analysis, which is available for public inspection and available online at www.hud.gov/respa.

Introduction

This chapter of the Regulatory Impact Analysis is the Final Regulatory Flexibility Analysis (FRFA) of the final rule as described under Section 604 of the Regulatory Flexibility Act. The requirements of the FRFA are listed below along with references to where the requirements are covered in the FRFA and where more detailed discussion can be found in other chapters of the Regulatory Impact Analysis (RIA).

A. A description of the reasons why action by the agency is being considered can be found in Section III of this chapter, in Section II of Chapter 1 of the RIA, and in greater detail in the first sections of Chapters 3 and 4 of the RIA.

B. A succinct statement of the objectives of, and legal basis for, the final rule is provided in Section III of this chapter. This is also discussed in Section II of Chapter 1 of the RIA and in greater detail in the first sections of Chapters 3 and 4 of the RIA.

C. A description and an estimate of the number of small entities to which the rule will apply or an explanation of why no such estimate is available. Section V provides data on small businesses that may be affected by the rule. As explained in Section V, Chapter 5 of the RIA also provides extensive documentation of the characteristics of the industries directly affected by the rule, including various estimates of the numbers

of small entities, reasons why various data elements are not reliable or unavailable, and descriptions of methodologies used to estimate (if possible) necessary data elements that were not readily available. The industries discussed in Chapter 5 of the RIA included the following (with section reference): mortgage brokers (Section II); lenders including commercial banks, thrifts, mortgage banks, credit unions (Section III); settlement and title services including direct title insurance carriers, title agents, escrow firms, and lawyers (Section IV); and other third-party settlement providers including appraisers, surveyors, pest inspectors, and credit bureaus (Section V); and real estate agents (Section VI). As explained in Section V of this chapter, Appendix A includes estimates of revenue impacts for the new Good Faith Estimate (GFE).

D. A description of the projected reporting, record keeping, and other compliance requirements of the rule, including an estimate of the classes of small entities that will be subject to the requirement and the types of professional skills necessary for preparation of the report or record. Compliance requirements and costs are discussed in Sections VII through IX of this chapter. In no case are any professional skills required for reporting, record keeping, and other compliance requirements of this rule that are not otherwise required in the ordinary course of business of firms affected by the rule. As noted above, Chapter 5 of the RIA includes estimates of the small entities that may be affected by the rule.

E. An identification, to the extent practicable, of all relevant Federal rules which may duplicate, overlap or conflict with the final rule. The final rule provisions describing some loan terms in the new GFE and the HUD-1 are similar to the Truth in Lending Act (TILA) regulations; however the differences in approach between the TILA

regulations and HUD's RESPA rule make them more complementary than duplicative. Overlaps are discussed further in this chapter.

In addition, this Chapter contains (c) a description of any significant alternatives to the final rule which accomplish the stated objectives of applicable statutes and which minimize any significant impact of the final rule on small entities. The FRFA also describes comments dealing with compliance and regulatory burden in the 2008 proposed rule. Some of the comments were on provisions of the 2008 proposed rule that have been dropped. Other comments were on impacts that the Department believes will be small or non-existent. Some of the compliance and regulatory burden comments concerned costs that are only felt during the start-up period and are one-time costs. These are discussed in Section VII.B, while comments on recurring costs of implementing the new GFE form are addressed in Section VII.C. Section VII.D discusses GFE-related changes in the final rule that reduce regulatory burden. Section VII.E discusses compliance issues related to GFE tolerances on settlement party costs, while Section VII.F discusses efficiencies associated with the new GFE.

Before proceeding further, Section II provides a brief summary of the main findings from the Regulatory Impact Analysis that relate to the final rule.

Summary of the Regulatory Impact Analysis

There is strong evidence of information asymmetry between mortgage originators and settlement service providers and consumers, allowing loan originators to capture much of the consumer surplus in this market through price discrimination. The RESPA disclosure statute is meant to address this information asymmetry, but the evidence shows that the current RESPA regulations are not effective. The final rule will create a more

level-playing field through a more transparent and standard disclosure of loan details and settlement costs; tolerances on settlement charges leading to prices that consumers can rely on; and a comparison page on the HUD-1 that allows the consumer to compare the amounts listed for particular settlement costs on the GFE with the total costs listed for those charges on the HUD-1, and to double check the loan details at settlement double check the loan details at settlement. These changes will encourage comparison shopping by informed consumers, which will place a competitive pressure on market prices, and enable consumers to retain more consumer surplus.

Overview of Final Rule

The Department of Housing and Urban Development has issued a final rule under the Real Estate Settlement Procedures Act (RESPA) to simplify and improve the process of obtaining home mortgages and to reduce settlement costs for consumers. This Regulatory Impact Analysis and Regulatory Flexibility Analysis examine the economic effects of that rule. As this Regulatory Impact Analysis demonstrates, the final rule is expected to improve consumer shopping for mortgages and to reduce the costs of closing a mortgage transaction for the consumer. Consumer savings were estimated under a variety of scenarios about originator and settlement costs. In the base case, the estimated price reduction to borrowers comes to $8.35 billion or $668 per loan. This represents the substantial savings that can be achieved with the final rule.

The final RESPA rule includes a new, simplified Good Faith Estimate (GFE) that includes tolerances on final settlement costs and a new method for reporting wholesale lender payments in broker transactions. The final rule allows service providers to use prices based on the average charges for the third-party services they purchase, making

their business operations simpler and less costly. Competition among loan originators will put pressure for these cost savings to be passed on to borrowers. The new GFE will produce substantial shopping and price-reduction benefits for both origination and third-party settlement services.

Because the final rule calls for significant changes in the process of originating a mortgage, this Regulatory Impact Analysis identifies a wide range of benefits, costs, efficiencies, transfers, and market impacts. The effects on consumers from improved borrower shopping will be substantial under this rule. Similarly, the use of tolerances will place needed controls on origination and third-party fees. Ensuring that yield spread premiums are credited to borrowers in brokered transactions could cause significant transfers to consumers. The increased competition associated with RESPA reform will reduce settlement service costs and result in transfers to consumers from service providers. Entities that will suffer revenue losses under the final rule are usually those who are charging prices higher than necessary or are benefiting from the current system's market failure.

Note to Reader: A comprehensive summary of the problems with the current mortgage shopping system and the benefits and market impacts of the final rule is provided in Section I of Chapter 3.

Problems with the Mortgage Shopping Process and the Current GFE

The current system for originating and closing mortgages is highly complex and suffers from several problems that have resulted in high prices for borrowers. Studies indicate that consumers are often charged high fees and can face wide variations in

prices, both for origination and third-party settlement services. The main points are as follows:

- There are many barriers to effective shopping for mortgages in today's market. The process can be complex and can involve rather complicated financial trade-offs, which are often not fully and clearly explained to borrowers.

- Consumers often pay non-competitive fees for originating mortgages. Most observers believe that the market breakdown occurs in the relationship between the consumer and the loan originator -- the ability of the loan originator to price discriminate among different types of consumers leads to some consumers paying more than other consumers.[1]

- There is convincing statistical evidence that yield spread premiums are not always used to offset the origination and settlement costs of the consumer. Studies, including a recent HUD-sponsored study of FHA closing costs by the Urban Institute, find that yield spread premiums are often used for the originator's benefit, rather than for the consumer's benefit.[2]

- Borrowers can be confused about the trade-off between interest rates and closing costs. It may be difficult for borrowers (even sophisticated ones but surely unsophisticated ones) to understand the financial trade-offs associated with discount points, yield spread premiums, and upfront settlement costs. While

[1] One could see price discrimination in a competitive market that was the result of different costs associated with originating loans for different applicants. For example, those who required more work by the originator to obtain loan approval might be charged more than those whose applications required little work in order to obtain an approval. The price discrimination we refer to in this paragraph and elsewhere in this analysis is not cost-based. It is the result of market imperfections, such as poor borrower information on alternatives that leads borrowers to accept loans at higher cost than the competitive level.
[2] See Section IV.D of Chapter 2 for a discussion of these studies.

many originators explain this to their borrowers, giving them an array of choices to meet their needs, some originators may only show borrowers a limited number of options.

- There is also evidence that prices paid for third-party services are highly variable, indicating that there is much potential to reduce title, closing, and other settlement costs. For example, a recent analysis of FHA closing costs by the Urban Institute shows wide variation in title and settlement costs. There is not always an incentive in today's market for originators to control these costs. Too often, high third-party costs are simply passed through to the consumer. And consumers may not be the best shoppers for third-party service providers due to their lack of expertise and to the infrequency with which they shop for these services. Consumers often rely on recommendations from the real estate agent (in the case of a home purchase) or from the loan originator (in the case of a refinance as well as a home purchase).

Today's GFE. Today's GFE does not help the above situations, as it is not an effective tool for facilitating borrower shopping nor for controlling third-party settlement costs. The current GFE is typically comprised of a long list of charges, as today's rules do not prescribe a standard form or consolidated categories. Such a long list of individual charges can be overwhelming, often confuses consumers, and seems to provide little useful information for consumer shopping. The current GFE certainly does not inform consumers what the major costs are so that they can effectively shop and compare mortgage offers among different loan originators. The current GFE does not explain how the borrower can use the document to shop and compare loans. Also, the GFE fails to

make clear the relationship between the closing costs and the interest rate on a loan, notwithstanding that many mortgage loans originated today adjust up-front closing costs due at settlement, either up or down, depending on whether the interest rate on the loan is below or above "par." Finally, current rules do not assure that the "good faith estimate" is a reliable estimate of final settlement costs. As a result, under today's rules, the estimated costs on GFEs may be unreliable or incomplete, and final charges at settlement may include significant increases in items that were estimated on the GFE, as well as additional fees, which can add to the consumer's ultimate closing costs.

Thus, today's GFE is not an effective tool for facilitating borrower shopping or for controlling origination and third-party settlement costs. There is enormous potential for cost reductions in today's market, which is too often characterized by relatively high and highly variable charges for both origination and third-party services.

In addition, today's RESPA rules hold back efficiency and competition by acting as a barrier to innovative cost-reduction arrangements. While today's mortgage market is characterized by increased efficiencies and lower prices due to technological advances and other innovations that is not the case in the settlement area where aggressive competition among settlement service providers simply does not always take place. Existing RESPA regulations inhibit average cost pricing,[3] which is an example of a cost reduction technique. Thus, a framework is needed that would encourage competitive

[3] The charges reported on the HUD-1 are required to be the specific charge paid in connection with the specific loan for which the HUD-1 is filled out. Pricing based on average charges is the practice of charging all borrowers the same average charge for a group of similar loans. Average cost pricing requires less record keeping and tracking for any individual loan since the numbers reported to the settlement agent need not be transaction specific. Average cost pricing is not permissible under RESPA because loan-specific prices are required.

negotiations and other arrangements that would lead to lower settlement prices. The new GFE will provide such a framework.

Approach of the Final Rule

Main Components of the New GFE and HUD-1

The GFE format simplifies the process of originating mortgages by consolidating costs into a few major cost categories.[4] The GFE ensures that in brokered transactions, borrowers receive the full benefit of the higher price paid by wholesale lenders for a loan with a high interest rate; that is, so-called yield spread premiums. On both the GFE and HUD-1, the portion of any wholesale lender payments that arise because a loan has an above-par interest rate is passed through to borrowers as a credit against other costs. Thus, there is assurance that borrowers who take on an above-par loan receive funds to offset their settlement costs. The new GFE also includes a trade-off table that will assist consumers in understanding the relationship between higher interest rates and lower settlement costs.

HUD conducted consumer tests to further improve the GFE form in the 2002 proposed rule. Numerous changes were made to make the GFE more user-friendly. The GFE form in the final rule includes a summary page containing the key information for shopping; during the tests, consumers reported that the summary page was a useful addition to the GFE. The trade-off table, another component of the GFE that consumers found useful, is also included in the final GFE. The final GFE is a form that consumers find to be clear and well written and, according the tests conducted, one that they can use to determine the least expensive loan. In other words, it is a shopping tool that is a vast

[4] See the proposed GFE in Exhibit 3-B of Chapter 3.

improvement over today's GFE with its long list of fees that can change (i.e., increase) at settlement.

The final GFE includes a set of tolerances on originator and third-party costs: originators must adhere to their own origination fees, and give estimates subject to a 10 percent upper limit on the sum of certain third-party fees. The tolerances on originator and third-party costs will encourage originators not only to lower their own costs but also to seek lower costs for third-party services.

The final rule would allow service providers to use pricing based on average charges for third-party services they purchase so long as the average is calculated using a documented method and the charge on the HUD-1 is no greater than the average paid for that service. This will make internal operations for the loan originator simpler and less costly and competition among lenders will put pressure for these cost savings to be passed on to borrowers as well. The end result of all these changes should be lower third-party fees for consumers.

To increase the value of the new GFE as a shopping document, HUD is proposing revisions to the HUD-1 Settlement Statement form that will make the GFE and HUD-1 easier to compare. The revised HUD-1 uses the same language to describe categories of charges as the GFE, and orders the categories of charges in the same way. This makes it much simpler to compare the two documents and confirm whether the tolerances required in the new GFE have been met or exceeded. In addition, the final rule introduces a comparison in the revised HUD-1 that would: (1) compare the GFE estimates to the HUD-1 charges and advise borrowers whether tolerances have been met or exceeded; (2) verify that the loan terms summarized on the GFE match those in the loan documents,

including the mortgage note; and (3) provide additional information on the terms and conditions of the mortgage. These components of the rule are required together to fully realize the consumer saving on mortgage closing cost estimated here.

Given that there has been no significant change in the basic HUD-1 structure and layout, besides the addition of a comparison page, generating this new HUD-1 should not pose any problem for firms closing loans -- in fact, the closing process will be much simpler given that borrowers and closing agents can precisely link the information on the initial GFE to the information on the final HUD-1.The HUD-1 has also been adjusted to ensure that the new GFE (a shopping document issued early in the process) and the HUD-1 (a final settlement document issued at closing) work well together. The layout of the revised HUD-1 has new labeling of some lines so that each entry from the GFE can be found on the revised HUD-1 with the exact wording as on the GFE. This will make it much easier to determine if the fees actually paid at settlement are consistent with the GFE, whether the borrower does it alone or with the assistance of the settlement agent. The reduced number of HUD-1 entries that should result, as well as use of the same terminology on both forms should reduce the time spent by the borrower and settlement agents comparing and checking the numbers.

The significant changes made to the final rule from the March 2008 proposed rule are:

- A GFE form that is a shorter form than had been proposed.
- Allowing originators the option not to fill out the tradeoff table on the GFE form.

- A revised definition of application to eliminate the separate GFE application process.
- Adoption of requirements for the GFE that are similar to recently revised Federal Reserve Board Truth-in-Lending regulations which limit fees charged in connection with early disclosures and defining timely provision of the disclosures.
- Clarification of terminology that describes the process applicable to, and the terms of, an applicant's particular loan.
- Inclusion of a provision to allow lenders a short period of time in which to correct certain violations of the new disclosure requirements.
- A revised HUD-1/1A settlement statement form that includes a summary page of information that provides a comparison of the GFE and HUD-1/1A list of charges and a listing of final loan terms as a substitute for the proposed closing script addition.
- Elimination of the requirement for a closing script to be completed and read by the closing agent.
- A simplified process for utilizing an average charge mechanism.
- No regulatory change in this rulemaking regarding negotiated discounts, including volume based discounts.

Estimates and Sources of Consumer Savings from the Final Rule

Overall Savings. Chapter 3 discusses the consumer benefits associated with the new GFE form and provides dollar estimates of consumer savings due to improved shopping for both originator and third-party services. Consumer savings were estimated under a variety of scenarios about originator and settlement costs.[5] In the base case, the estimated price reduction to borrowers comes to $8.35 billion annually, or 12.5 percent of the $66.7 billion in total charges (i.e., origination fees, appraisal, credit report, tax service and flood certificate and title insurance and settlement agent charges).[6] Thus, there is an estimated $8.35 billion in transfers from firms to borrowers from the improved disclosures and tolerances of the new GFE. This would represent savings of $668 per loan. Sensitivity analysis was conducted with respect to the savings projection in order to provide a range of estimates. Because title fees account for over 70 percent of third-party fees and because there is widespread evidence of lack of competition and overcharging in the title and settlement closing industry, one approach projected third-party savings only in that industry. This approach (called the "title approach") projected savings of $200 per loan in title and settlement fees. In this case, the estimated price reduction to borrowers comes to $8.38 billion ($670 per loan), or 12.6 percent of the $66.7 billion in total charges – savings figures that are practically identical to the base case mentioned above.[7] Other projections also showed substantial savings for consumers. As explained in Chapter 3, estimated consumer savings under a more conservative projection totaled

[5] Throughout this Economic Analysis, the terms "borrowers" and "consumers" are often used interchangeably.
[6] Government fees and taxes and escrow items are not included in this analysis, as they are not subject to competitive market pressures.
[7] If the savings in title and settlement closing fees due to RESPA reform were only $150, then the estimated price reduction to borrowers comes to $7.76 billion, or 11.6 percent of the $66.7 billion in total charges.

$6.48 billion ($518 per loan), or 9.7 percent of total settlement charges. Thus, while consumer savings are expected to be $8.35 billion (or 12.5 percent of total charges) in the base case or $8.38 billion (12.6 percent of total charges) in the title approach, they were $6.48 billion (or 9.7 percent of total charges) in a more conservative sensitivity analysis. This $6.48-$8.38 billion ($518 - $670 per loan) represents the substantial savings that can be achieved with the new GFE.

Industry Breakdown of Savings. Chapter 3 also disaggregates the sources of consumer savings into the following major categories: originators with a breakdown for brokers and lenders, and third-party providers with a breakdown for the title and settlement industry and other third-party providers.[8] In the base case, originators (brokers and lenders) contribute $5.88 billion, or 70 percent of the $8.35 billion in consumer savings. This $5.88 billion in savings represents 14.0 percent of the total revenue of originators, which is projected to be $42.0 billion.[9] The $5.88 billion is divided between brokers, which contribute $3.53 billion, and lenders (banks, thrifts, and mortgage banks), which contribute the remaining $2.35 billion. The shares for brokers (60 percent) and lenders (40 percent) represent their respective shares of mortgage originations.

In the base case, third-party settlement service providers contribute $2.47 billion, or 30 percent of the $8.35 billion in consumer savings. This $2.47 billion in savings represents 10.0 percent of the total revenue of third-party providers, which is projected to be

[8] Readers are referred to Chapter 5 for a more detailed examination of the various component industries (e.g., title services, appraisal, etc.) as well as for the derivations of many of the estimates presented in this chapter.

[9] This assumes a 1.75 percent origination fee for brokers and lenders, which, when applied to projected originations of $2.4 trillion, yields $42.0 billion in total revenues from origination fees (both direct and indirect). See Steps (3)-(5) of Section VII.E.1 of Chapter 3 for the explanation of origination costs. Sensitivity analyses are conducted for smaller origination fees of 1.5 percent and larger fees of 2.0 percent; see Step (21) in Section VII.E.4 of Chapter 3.

$24.738 billion.[10] The $2.47 billion is divided between title and settlement agents, which contribute $1.79 billion, and other third-party providers (appraisers, surveyors, pest inspectors, etc.), which contribute $0.68 billion. Title and settlement agents contribute a large share because they account for 72.5 percent of the third-party services included in this analysis. In the title approach, title and settlement agents account for all third-party savings, which total $2.5 billion if per loan savings are $200 and $1.88 billion if per loan savings are $150.

Table 6-1. Industry Breakdown of Consumer Savings

Source of Savings	**Transfers (billions)**	**Savings per loan (12.5 million loans)**	**Percentage of Total Savings**
Loan Origination	**$5.88**	**$470**	**70%**
Lenders	**$2.35**	**$470 or**	**28%**
Brokers	**$3.53**	**$470**	**42%**
Third-Party Services	**$2.47**	**$198**	**30%**
Title/Settlement	**$1.79**	**$143**	**22%**
Other	**$0.68**	**$54**	**8%**
Total*	**$8.35**	**$668**	**100%**

***Savings are 12.5% of $66.7 billion revenue in charges.**

Section III.D of this executive summary presents the revenue impacts on small originators and small third-party providers.

[10] See Step (7) of Section VII.E.1 of Chapter 3 for the derivation of the $24.738 billion.

Sources of Savings: Lower Origination and Third-Party Fees. The Regulatory Impact Analysis presents evidence that some consumers are paying higher prices for origination and third-party services. The new GFE format in the final rule will improve consumer shopping for mortgages, which will result in better mortgage products, lower interest rates, and lower origination and third-party costs for borrowers.

- The final rule simplifies the process of originating mortgages by consolidating costs into a few major cost categories. This is a substantial improvement over today's GFE that is not standardized and can contain a long list of individual charges that encourages fee proliferation. This makes it easier for the consumer to become overwhelmed and confused. The consistent and simpler presentation of the GFE will improve the ability of the consumer to shop.

- A GFE with a summary page, which includes the terms of the loan, will make it clear to the consumer whether they are comparing similar loans.

- A GFE with a summary page will make it simpler for borrowers to shop. The higher reward for shopping, along with the increased ease with which borrowers can compare loans, should lead to more effective shopping, more competition, and lower prices for borrowers.

- The GFE makes cost estimates more reliable by applying tolerances to the figures reported. This will reduce the all too frequent problem of borrowers being surprised by additional costs at settlement. With fees firmer under the GFE, shopping is more likely to result in borrowers saving money when they shop.

- The new GFE will disclose yield spread premiums and discount points in brokered loans prominently, accurately, and in a way that should inform borrowers how they may be used to their advantage. Both values will have to be calculated as the difference between the wholesale price of the loan and its par value. Their placement in the calculations that lead to net settlement costs will make them very difficult to miss. That placement should also enhance borrower comprehension of how yield spread premiums can be used to reduce up-front settlement costs. Tests of the form indicate that consumers can determine the cheaper loan when comparing a broker loan with a lender loan.

- The new GFE will better inform consumers about their financing choices by including a tradeoff table on page 3 where originators can present the different interest rate and closing cost options available to borrowers. For example, consumers will better understand the trade-offs between reducing their closing costs and increasing the interest rate on the mortgage.

- The final rule allows settlement service providers to use prices based on average charges for the third-party services they purchase.

- The above changes and the imposition of tolerances on fees will encourage originators to seek lower settlement service prices. The tolerances will lead to well-informed market professionals either arranging for the purchase of the settlement services or at least establishing a benchmark that borrowers can use to start their own search. Under either set of circumstances, this should lead to

lower prices for borrowers than if the borrowers shopped on their own, since the typical borrower's knowledge of the settlement service market is limited, at best.

Savings and Transfers, Efficiencies, and Costs

As explained above, it is estimated that borrowers would save $8.35 billion in origination and settlement charges. This $8.35 billion represents transfers to borrowers from high priced producers, with $5.88 billion coming from originators and $2.47 billion from third-party settlement service providers. In addition to the transfers, there are efficiencies associated with the rule as well as costs.

Mortgage applicants and borrowers realize $1,169 million savings in time spent shopping for loans and third-party services. Loan originators save $975 million in time spent with shoppers and from average cost pricing. Third-party settlement service providers save $191 million in time spent with shoppers. Some or all of industry's total of $1,166 million in efficiency gains have the potential to be passed through to borrowers through competition. There are additional social efficiencies such as the reduction of non-productive behavior and positive externalities of preventing foreclosures (see Section X.D.).

The total one-time compliance costs to the lending and settlement industry of the GFE and HUD-1 are estimated to be $571 million, $407 million of which is borne by small business. These costs are summarized below. Total recurring costs are estimated to be $918 million annually or $73.40 per loan. The share of the recurring costs on small business is $471 million. This Chapter 6 examines in greater detail the compliance and other costs associated with the GFE and HUD-1 forms and its tolerances.

The new GFE in the final rule has some features that would increase the cost of providing it and some that would decrease the cost. Practically all of the information required on the GFE is readily available to originators, suggesting no additional costs. The fact that there are fewer numbers and less itemization of individual fees suggests reduced costs. On the other hand, there could be a small amount of additional costs associated with the optional trade-off table but that is not clear. Thus, while it is difficult to estimate, it appears that there could be a net of zero additional costs. However, if the GFE added 10 minutes per application to the time it takes to handle the forms today; annual costs would rise by $255 million at 1.7 application per loan or ($12 per application or $20 per loan) or $405 million at 2.7 applications per loan ($32 per loan). We assume the high-cost scenario for summary table 6-5 (See Section VII.C.1 of this chapter for further details.)

The presence of tolerances will lead to some additional costs to originators of making additional arrangements for third parties to provide settlement services. If the average loan originator incurs an average of 10 minutes per loan of effort making third-party arrangements to meet the tolerances, then the total cost to originators of making third-party arrangements to meet the tolerance requirements comes to $150 million ($12 per loan). (See Section VII.E.2 of this chapter.)

There is the potential of additional underwriting costs if the number of applications requiring a credit check rise beyond the current ratio of 1.7 applications per loan. Thus, if this ratio remains constant, there will be no recurring compliance costs from additional underwriting. If, however, the demand for preliminary GFEs increases

to 2.7 applications per loan, then the total costs for originators will be $138 million or $11 per loan (See Section VII.C.).

In addition to the recurring costs of the GFE, there will be one-time adjustment costs of $383 million in switching to the new form. Loan originators will have to upgrade their software and train staff in its use in order to accommodate the requirements of the new rule. It is estimated that the software cost will be $33 million and the training cost will be $58 million, for a total of $91 million (see Section VII.B.1 of this chapter). We assume that, of the loan originators' software and training costs, $73 million is attributable to the new GFE and $18 million to the new HUD-1. Once the new software is functioning, the recurring costs of training new employees in its use and the costs associated with periodic upgrades simply replace those costs that would have been incurred doing the same thing with software for the old rule. They represent no additional costs of the new rule.

Similarly, there will be a one-time adjustment cost for legal advice on how to deal with the changes related to the new GFE. The one-time adjustment cost for legal fees is estimated to be $116 million (see Section VII.B.2 of this chapter). Once the adjustment has been made, the ongoing legal costs are a substitute for the ongoing legal costs that would have been incurred under the old rule and do not represent any additional burden.

Finally with respect to the GFE, employees will have to be trained in the new GFE beyond the software and legal training already mentioned. This one time adjustment cost is estimated to be $194 million (see section VII.B.3). Again, once the transition expenses have been incurred, any ongoing training costs are a substitute for the

training costs that would have been incurred anyway and do not represent an additional burden.

There are few recurring costs associated with the revised HUD-1. For originators the burden could be very small: loan originators will not have to collect additional data beyond what is required for the GFE. In certain cases, the burden may be noticeable so we assume that the average burden is ten minutes per loan for loan originators. Settlement agents may face a recurring cost, although this is not likely either since loan originators are responsible for providing the data. The settlement agent will have to add final charges not known by the originator, and may have to fill out the entire form if the lender does not transmit the information on an already completed HUD-1 page 3. The settlement agent may also want to check the information concerning settlement costs, tolerances, and loan terms to make sure they agree with the GFE. In some cases, the settlement agent will have to calculate the tolerances. We assume that it will add five minutes on average to the time it takes to prepare a settlement. The actual distribution of the total additional time burden will differ by transaction depending on how much of the work is done by the lender. Taking loan originators into account, the total time burden is 15 minutes per loan, for a cost of $18 per loan. The recurring compliance cost to the industry would be $225 million annually, of which small business would bear $107 million annually. During a high-volume year (15.5 million loans annually), the annual recurring compliance cost of the HUD-1 would be $279 million annually (see Section VIII.C. of Chapter 6)

There will be one-time adjustment costs of $188 million in switching to the new HUD-1 form. Settlement firms will have to upgrade their software and train staff in its

use in order to accommodate the requirements of the new rule. It is estimated that the software and training cost will be $80 million (see Section VIII.B. of Chapter 6). Once the new software is functioning, the recurring costs of training new employees in its use and the costs associated with periodic upgrades simply replace those costs that would have been incurred doing the same thing with software for the old rule. They represent no additional costs of the new rule.

Table 6-2. Summary of One-Time Adjustment Costs (in millions)

	GFE		HUD-1		Total	
Source of Cost	All Firms	Small Firms	All Firms	Small Firms	All Firms	Small Firms
Software and training	$73	$52	$80	$59	$153	$111
Legal consultation	$116	$70	$37	$18	$153	$88
Training on rule	$194	$146	$71	$62	$265	$208
Total	$383	$268	$188	$139	$571	$407

Similarly, there will be a one-time adjustment cost for legal advice on how to deal with the changes related to the new HUD-1. The one-time adjustment cost for legal fees is estimated to be $37 million (see Section VIII.B. of Chapter 6). Once the adjustment has been made, the ongoing legal costs are a substitute for the ongoing legal costs that would have been incurred under the old rule and do not represent any additional burden.

Finally, employees will have to be trained in the new HUD-1 beyond the software and legal training already mentioned. This one time adjustment cost is estimated to be $71 million (see Section VIII.B. of Chapter 6). Again, once the transition expenses have

been incurred, any ongoing training costs are a substitute for the training costs that would have been incurred anyway and do not represent an additional burden.

The consumer savings, efficiencies and costs associated with the GFE are discussed further in Chapter 6 and in Chapters 3. A summary of the compliance costs for the base case of 12.5 million loans annually is presented below in Table 6.1.

Table 6-3. Compliance Costs of the Final Rule (if 12.5 million loans annually)

	One-time Compliance Costs incurred during the first year (in millions)		Recurring Compliance Costs (in millions annually)		$ cost per
	All Firms	Small Firms	All Firms	Small Firms	loan
GFE	$383	$268	$693	$364	$55.40
HUD-1	$188	$139	$225	$107	$18.00
Total	$571	$407	$918	$471	$73.40

A natural question to raise is whether the costs of the rule will overwhelm the benefits of the rule. The assumption that consumers will benefit by a reduction of settlement costs of at least $668 per loan has not been forcefully challenged. Indeed, results from a recent statistical analysis of FHA data imply that the savings to consumers may be as much as $1,200 per loan. To accomplish this, however, industry will incur both adjustment and recurring costs. Suppose firms impose these additional costs on consumers by raising prices. It is likely that the adjustment costs will be spread out over many years, just as the cost of an investment would be. Suppose, for the sake of illustration, that all adjustment costs are all imposed on first-year borrowers only. In a normal year of 12.5 million loans, this cost would $46 per loan. The recurring

compliance costs of the rule is $73.40 per loan regardless of the year. In such a scenario, the total compliance cost is $120 per loan in the first year as compared to $74 for later years. If all compliance costs were passed onto consumers then the net consumer savings is $548 the first year and $594 in subsequent years (see table 6-4 for a summary). Note that this assumes that all costs are borne by borrowers and not at all by the applicants who do not get a loan. It would be reasonable to assume that in the high-application scenario, where there is an increase in preliminary underwriting costs, that the cost of an initial credit report would be passed on to all applicants.

Table 6-4. Predicted Reductions in the Cost of a Loan

(if firms impose all first-year adjustment costs on first-year borrowers)

Source of Gain or Loss	First Year	Afterwards
Average Consumer Savings	$668	$668
One-time Adjustment Costs	-$46	-$0
Recurring Compliance Costs	-$74	-$74
Net Consumer Savings	$548	$594
Firms' Efficiencies	+$93	+$93
Borrowers' Efficiencies	+$55	+$55
Net Benefits to Consumer	$696	$742

There are other potential benefits to the consumer besides savings on settlement costs. There are aspects of this rule that will save time for industry. The value of these efficiencies could be $1,166 million for loan originators and settlement agents, for a per loan efficiency of $93. In a competitive industry, firms would pass these gains along to borrowers in the form of lower costs, a consumer benefit. Borrowers themselves will

save time through the new GFE. These time savings are estimated at $1,169 million but are derived from a time savings worth $55 per applicant (seventy-five minutes at $44 per hour). In the summary of net benefits, we only include the per applicant time savings for borrowers. We make the cautious assumption that successful borrowers have submitted only one application. A fraction of the additional 8.25 million applications (in excess of 12.5 million loans) consist of: applications approved but not accepted; applications denied by the financial institution; and applications withdrawn by the applicant. Although these individuals also realize time savings, it would be misleading to include them in a "per loan" figure in that the time savings of rejected applicant would not benefit the borrower. Adding the firms' and borrowers' value of time efficiencies to the net of compliance cost consumer savings gives us an estimate of the potential consumer benefits per loan: $696 in the first year and $742 afterwards.

Alternatives Considered to Make the GFE More Workable for Small and Other Businesses

Chapter 3 discusses the many comments that HUD received on the GFE in the 2002 and 2008 proposed rules and the 2005 RESPA Reform Roundtables. Chapter 4 discusses alternatives. The most basic alternative was to make no change in the current GFE. The final rule allows both the current GFE and the new GFE to be used for one year after the GFE is introduced, but requires the new GFE and HUD-1 to be used beginning January 1, 2010. This approximately one-year adjustment period responds to lenders' comments that there would be significant implementation issues with switching to a new GFE.

The main alternative concerning small businesses considered the brokers' argument that they were disadvantaged by the reporting of yield spread premiums. The new GFE was designed to ensure that there will not be any anti-competitive impacts on the broker industry. A summary page is included that presents the key cost figures for borrower shopping that does not report yield spread premiums, and that provides identical treatment for brokers and lenders. The final GFE includes language that clarifies how yield spread premiums reduce the upfront charge that borrowers pay. Section III.E of this Executive Summary discusses this in more detail.

HUD designed the GFE to make it workable for small lenders and brokers. Some examples of the changes are the following:

- In response to concerns expressed by lenders and brokers about their ability to control third-party costs and meet the specified tolerances in the 2008 proposed rule, HUD raised the tolerance on government recording charges from zero to ten percent.

- Consistent with the above, the rule creates a new definition of "forseeable circumstances" that clarifies and expands on the definition of "circumstances" in the proposed rule. For example, material information that was either not known at the time the original GFE was provided or not relied on in providing the original GFE, or information that has changed in a material way since application, may be the basis for providing a modified GFE. For example, if the actual loan amount turns out to be higher than the loan amount indicated by the borrower at the time the GFE was provided, and certain settlement charges that are based on the loan amount increase as a result, the loan originator may provide a revised

GFE reflecting those higher amounts. Compliance with the tolerance provisions would be evaluated by comparing the revised GFE with the actual amounts charged at settlement.

- HUD has adopted a streamlined single application process for the final rule. The new definition will allow loan originators more flexibility in determining the information they need to underwrite a GFE.

- The reading at settlement of a closing script is no longer required. Much of the same information will be transmitted to the borrower via a new page 3 of the HUD-1.

Alternatives. This chapter and Chapter 4 and Chapter 6 discuss other major alternatives that HUD considered in developing the final rule from the 2008 proposed rule. These chapters discuss the pros and cons of these alternatives and why HUD decided not to include them in this final rule.

Market and Competitive Impacts on Small Businesses from the Final Rule

Transfers from Small Businesses. It is estimated that $4.13 billion, or 49.5 percent of the $8.35 billion in consumer savings comes from small businesses, with small originators contributing $3.01 billion and small third-party firms, $1.13 billion.[11] Within the small originator group, most of the transfers to consumers come from small brokers ($2.47 billion, or 82 percent of the $3.01 billion); this is because small firms account for most of broker revenues but a small percentage of lender revenues. Within the small third-party group, most of the transfers come from the title and closing industry ($0.68

[11] In the more conservative scenario of $6.48 billion in consumer savings, small businesses would account for $3.21 billion of the transfers to consumers, with small originators accounting for $2.36 billion, and small third-party providers, $0.84 billion.

billion, or 60 percent of the $1.13 billion), mainly because this industry accounts for most third-party fees. In the title approach, small title and settlement closing companies account for $0.95 billion of the $2.5 billion in savings. Section VII.E.2 of Chapter 3 explains the steps in deriving these revenue impacts on small businesses, and Section VII.E.4 of Chapter 3 reports several sensitivity analyses around the estimates. In addition, Chapter 5 provides more detailed revenue impacts for the various component industries.[12]

The summary bullets in Section I.C highlight the mechanisms through which these transfers are expected to happen. Improved understanding of yield spread premiums, discount points, and the trade-off between interest rates and settlement costs; improved consumer shopping among originators; more aggressive competition by originators for settlement services; and increased competition associated with discounting -- all will lead to reductions in both originator and third-party fees. As noted earlier, there is substantial evidence of non-competitive prices charged to some in the origination and settlement of mortgages due to information asymmetry between originators and borrowers. Originators (both small and large) and settlement service providers (both small and large) that have been charging high prices will experience reductions in their revenues as a result of the new GFE. There is no evidence that small businesses have been disproportionately charging high prices; for this reason, there is no expectation of any disproportionate impact on small businesses from the new GFE. The revenue reductions will be distributed across firms based on their non-competitive price behavior.

[12] In Chapter 5, see Section II for brokers, Section III for the four lender groups (commercial banks, thrifts, mortgage banks, and credit unions), Section IV for the various title and settlement groups (large insurers, title and settlement agents, lawyers, and escrow firms), Section V.A for appraisers, Section V.B for surveyors, Section V.C for pest inspectors, and Section V.D for credit bureaus.

Small Brokers.[13] The main issue raised by the brokers concerned the treatment in the 2008 proposed rule of yield spread premiums on the proposed Good Faith Estimate. Mortgage Broker representatives asserted that the proposed mortgage broker disclosure would achieve the opposite result and would detract from the consumer's ability to understand and comparison shop. They recommended that lenders should be treated similarly to facilitate shopping and promote consumer understanding. The current final rule addresses the concern expressed by brokers that the reporting of yield spread premiums in the 2008 proposed rule would disadvantage them relative to lenders.

The Department hired forms development specialists, the Kleimann Communication Group, to analyze, test, and improve the forms. Starting with the GFE form proposed in 2002, they reworked the language and presentation of the yield spread premium to emphasize that it offsets other charges to reduce settlement charges, the cash needed to close the loan. The subjects tested seemed to like the trade-off table that shows the trade-off between the interest rate and up-front charges. It illustrates how yield spread premiums can reduce upfront charges. There is the summary page designed to simplify the digestion of the information on the form by including only the total estimated settlement charges from page two. This is the first page any potential borrower would see. It contains only the essentials for comparison-shopping and is simple: a standard set of yes-no questions describing the loan and a very simple summary of costs and the bottom line. Yield spread premiums are never mentioned here. Lender and broker loans get identical treatment on page 1. A mortgage shopping chart is included on page 3 of the GFE, to help borrowers comparison shop. Arrows were added to focus the

[13] Practically all (98.9%) of the 30,000-44,000 brokers qualify as a small business. The Bureau of Census reports that small brokers account for 70% of industry revenue.

borrower on overall charges, rather than one component. All of these features work against the borrower misinterpreting the different presentation of loan fees required of brokers vis-à-vis lenders.

HUD has designed the GFE form to focus borrowers on the right numbers so that competition is maintained between brokers and lenders. The forms adopted in the final rule were tested on hundreds of subjects. The tests indicate that borrowers who comparison shop will have little difficulty identifying the cheapest loan offered in the market whether from a broker or a lender.

We do not believe that the customer outreach function that brokers perform for wholesale lenders is going to change with RESPA reform. Wholesale lending, which has fueled the rise in mortgage originations over the past ten years, will continue to depend on brokers reaching out to consumer customers and supplying them with loans. Brokers play the key role in the upfront part of the mortgage process and this will continue with the final GFE.

RESPA reform is also not going to change the basic cost and efficiency advantages of brokers. Brokers have grown in market share and numbers because they can originate mortgages at lower costs than others. There is no indication that their cost competitiveness is going to change in the near future. Thus, brokers, as a group, will remain highly competitive actors in the mortgage market, as they have been in the past.

While there is no evidence to suggest any anti-competitive impact, there will be an impact on those brokers who are charging non-competitive prices. And there is convincing evidence that some brokers (as well as some lenders) overcharge consumers (see studies reviewed in Chapter 2). As emphasized throughout the Regulatory Impact

Analysis, the new GFE will lead to improved and more effective consumer shopping, for many reasons -- the new GFE is simple and easy to understand, it includes reliable cost estimates, it effectively discloses yield spread premiums and discounts in brokered loans without disadvantaging brokers, it provides a vehicle to show consumers options, and it explains the trade-off between closing costs and interests rates to aid in understanding of yield spread premiums. This increased shopping by consumers will reduce the revenues of those brokers who are charging non-competitive prices. Thus, the main impact on brokers (both small and large) of the final rule will be on those brokers (as well as other originators) who have been overcharging uninformed consumers, through the combination of high origination fees and yield spread premiums.[14] As noted above, small brokers are expected to experience $2.47 billion in reduced fees.

Small Lenders. Lenders include mortgage banks, commercial banks, credit unions, and thrift institutions.[15] There are over 10,000 lenders that would be affected by the RESPA rule, as well as almost 4,000 credit unions that originate mortgages. While two-thirds of the lenders qualify as a small business (as do four-fifths of the credit unions), these small originators account for only 23 percent of industry revenues. Thus, small lenders (including credit unions) account for only $540 million of the projected $2.35 billion in transfers from lenders.[16]

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[14] As explained throughout this chapter, it is anticipated that market competition, under this proposed GFE approach, will have a similar impact on those lenders (non-brokers) who have been overcharging consumers through a combination of high origination costs and yield spread premiums.

[15] While it is recognized that the business operations and objectives of these lender groups can differ – not only between the groups (a mortgage banker versus a portfolio lender) but even within a single group (a small community bank versus a large national bank) – they raised so many of the same issues that it is more useful to address them in one place.

[16] Section III of Chapter 5 describes the characteristics of these component industries (number of employees, size of firms, etc.), their mortgage origination activity, and the allocation of revenue impacts between large and small lenders. That section also explains that the small business share of revenue could vary from 20 percent to 26 percent

In general, there was less concern expressed by lenders (as compared with brokers) about potential anti-competitive impacts of the GFE on small businesses. Small lenders -- relative to both brokers and large lenders -- will remain highly competitive actors in the mortgage market, as they are today. Small mortgage banks, community banks and local savings institutions benefit from their knowledge of local settlement service providers and of the local mortgage market. Nothing in the final GFE rule changes that. Generally, lenders and their associations opposed the proposed GFE on the grounds that in their opinion the form is too lengthy and would only confuse borrowers. Lenders had numerous comments on most aspects of the 2008 proposed GFE form – some of them dealing with major issues such as the difficulty in predicting costs within a three day period and many dealing with practical and more technical issues. HUD responded to many of the issues and concerns raised by lenders; Sections V, VI, and VIII of Chapter 3 discuss lenders' comments and HUD's response.

Some lenders were concerned about their ability to produce firm cost estimates (even of their own fees) within a three-day period, given the complexity of the mortgage process. Lenders wanted clarification on their ability to make cost adjustments as a result of information they gain during the full underwriting process. The tolerances in the final rule require that lenders play a more active role in controlling third-party costs than they have in the past. However, some lenders emphasized that they have little control over fees of third-party settlement providers, while others seem to not anticipate problems in this regard. As explained in I.B above, the final rule made several adjustments to the tolerance rules, which should make them workable for lenders. In addition, the final rule

allows average cost pricing, which should help lenders reduce their costs. Practically all lenders wanted clarification on the definition of application, and HUD did that.

There will be an impact on those lenders (both large and small) who are charging non-competitive prices. Improved consumer shopping with the new GFE will reduce the revenues of those lenders who are charging non-competitive prices. Thus, as with brokers, the main negative impact on lenders (both small and large) of the new GFE will be on those lenders who have been overcharging uninformed consumers.

Small Title and Settlement Firms. The title and settlement industry -- which consists of large title insurers, title agents, escrow firms, lawyers, and others involved in the settlement process -- is expected to account for $1.79 billion of the $2.47 billion in third-party transfers under the GFE in the final rule. Within the title and settlement group, small firms are expected to account for 38.1 percent ($0.68 billion) of the transfers, although there is some uncertainty with this estimate.[17] Step (8) of Section VII.E of Chapter 3 conducts an analysis that projects all of the consumer savings in third-party costs coming from the title industry; evidence suggests there are more opportunities for price reductions in the title industry, as compared with other third-party industries. In this case, consumer savings in title costs ($150-$200 per loan) ranged from $1.88 billion to $2.50 billion. To a large extent, the title and closing industry is characterized by local firms providing services at constant returns to scale. The demand for the services of these local firms will continue under the final GFE.

Section VIII.C of Chapter 3 summarizes the key competitive issues for this industry with respect to the final rule. As noted there, the overall competitiveness of the

[17] Section IV of Chapter 5 describes the component industries and estimates the share of overall industry revenue going to small businesses.

title and closing industry should be enhanced by the RESPA rule. Chapters 2 and 5 provide evidence that title and closing fees are too high and that there is much potential for price reductions in this industry. Increased shopping by consumers, as well as increased shopping by loan originators to stay within their tolerances, will reduce the revenues of those title and closing companies that have been charging non-competitive prices.[18] Excess charges will be reduced and competition will ensure that reduced costs are passed through to consumers.

The title industry argued that greater itemization was needed in order for consumers to be able to adequately comparison shop among estimates. HUD's view is that the consolidated categories on the new GFE form provide consumers with the essential information needed for comparison-shopping. Itemization encourages long lists of fees that confuse borrowers.

It is important to keep in mind the local nature of the title industry when considering the impacts of the final RESPA reform (new GFE, tolerances, etc.) on the title industry. The title industry demonstrates a high degree of geographic specialization. Although title insurance companies do not need to be close to the properties insured, until there is widespread use of standardized electronic land record keeping accessible by the Internet,[19] the information-gathering service the industry provides will require proximity to land title records (or the establishment of "title plants," i.e., duplicates of local records, the maintenance of which requires proximity to local government records). Even if a

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[18] The reasons why the proposed GFE and its tolerances will lead to improved and more effective shopping for third-party services by consumers and loan originators has already been discussed, and need not be repeated here.

[19] The proposed rule does nothing to advance or retard this fundamental change in the nature of the business. It is possible that governments responsible for maintaining title records could advance to the level demonstrated in British Columbia (Canada), where even title insurance is not part of real estate transactions.

provider is efficient and charges low prices, it will not be able to compete against title and closing firms who are located sufficiently closer to the site in question. Thus, title and closing companies are by economic necessity provided by local firms. Reinforcing the local orientation are the value of local expertise and the importance of personal networks in receiving referrals.

The local orientation of the title industry could change over time. However, it is unlikely that RESPA reform would be the catalyst. The advances in technology that would change business practices are independent of what HUD does about RESPA. The only change that the final rule will introduce is that title and closing services may occur at lower prices negotiated between providers and lender originators. There will be no significant change in the local provision of title and closing work. Nor will there be a reduction of the number of these services purchased since this reform will not result in a drop in the number of mortgages that require these services. Large lenders will have to deal with multiple settlement services providers in order to ensure complete geographic coverage, and large multi-jurisdictional title firms have no apparent cost advantages over smaller title firms. In fact, large multi-jurisdictional title firms may have location-related cost disadvantages. There is no reason to believe that small title firms charging competitive prices will be adversely impacted by the changes in this rule. The demand for the services of these local firms will continue under the final GFE.

Appraisers. Like surveys and pest inspections, traditional appraisals are provided on-site at the mortgaged property. The transportation cost of visiting individual sites, especially the opportunity cost of the time spent in transit, adds substantially to the cost of providing the service. The transportation costs counterbalance, or overwhelm, any

scale economies that may otherwise exist in the production of these services. The countervailing transportation cost pressures creates an effective constant returns to scale production function for this industry and can serve to explain the wide range of firm size as well as the continued success of small businesses in the appraisal industry. This explains why approximately 99.8 percent of traditional appraisal firms qualify as small businesses.

Even if large appraisal firms are efficient and charges low prices, they will not have the same advantage as providers who are located sufficiently closer to the site in question. Thus, traditional appraisals are by economic necessity provided by local firms. Reinforcing the local orientation of the appraisal industry is the value of local expertise. A profound understanding of the characteristics of the local real estate market is essential for a successful appraisal. In addition, local appraisal firms maintain local networks of customers and clients, based on their established track records, which should give them a solid business advantage.

The local orientation of the appraisal industry could change over time. There has been a trend towards the increasing use of automated valuation appraisals, particularly for appraising properties that are being refinanced and properties that are being used as collateral for home equity loans. The necessity for appraisers to visit all homes in need of an appraisal could be rendered less by the automated value model (AVM), but it is also the case that the databases used to create AVMs tend not to have data on whether or not there is water in the basement of the subject property. It is unlikely that RESPA reform would be the catalyst for increases in AMVs, as the technological advances are already taking place. While RESPA reform could accelerate the use of AVMs, it will not likely

have an impact as to whether AVMs are eventually accepted more broadly by the lending industry. The adoption of AVMs will depend on the accuracy of these estimation models, their appropriateness for different types of properties, and their performance in mitigating the risk of default losses.

Statement of Need for and Objectives of the Rule[20]

Acquiring a mortgage is one of the most complex transactions a family will ever undertake. The consumer requires a level of financial sensibility to fully understand the product. For example, consider the trade-off between the yield spread premium and interest rate payments. Borrowers do not have access to the rate sheets that describe this trade-off. Indeed, many consumers may not even understand that there is a trade-off. To further complicate matters, the mortgage industry is continuously evolving: the range and complexity of products expands every year. Because consumers borrow fairly infrequently, the average borrower will be at an extreme informational disadvantage compared to the lender. To exacerbate this situation, the typical homebuyer may be rushed and easily steered into a bad loan because they are under pressure to make an offer on a home. This is especially the case for first-time homebuyers who will not be as likely to challenge lenders, whom they may view as unquestionable experts.

Closing costs (lender fees and title charges) add to the borrower's confusion. They are not as significant as the loan itself and total on average approximately four percent of the loan amount. However, the direct lender fees and the title charges are perhaps just as perplexing to the consumer. First, the multiplicity of fees is confusing (see Exhibits 1-3 of Chapter 3 for a list of the different names of upfront lender fees and

[20] For a detailed discussion of problems with the current system, and thus the need for this proposed rule, see Sections IV and V of Chapter 2 and Sections I and VII of Chapter 3.

settlement charges). The purpose of every fee and title charge is likely to be neither understood nor questioned by the average first-time homebuyer, who may be intimidated by the formality of the transaction. Second, to add to the confusion and uncertainty, even once the charges have been agreed upon, they are subject to change until the day of closing. Such informational asymmetries between the buyer and seller impede the ability of the consumer to be an effective shopper and negotiator.

Consumers have strong incentives to ensure that they are getting the best deal possible on a mortgage loan and the associated third-party settlement costs, but poorly-informed decisions have drastic consequences. First, the household itself will lose by paying more for housing and possibly by ruining their credit history in the event of default. Second, markets imperfections stemming from information asymmetries may stand in the way of achieving one of this administration's domestic priorities: expansion of homeownership. There is a wide range of positive economic externalities from homeownership that have been investigated in the empirical housing economics literature. These include household saving, wealth accumulation, property improvements, a more pleasing urban environment, an increase in political activity, a reduction of crime, better child outcomes, and a positive impact on the labor supply of women. The average loan amount is 3.5 times a household's income: even minor inefficiencies in this market will have sizeable impacts on the U.S. economy.

The current GFE format contains a long list of individual charges that can be overwhelming, often confuses consumers, and seems to provide little useful information for consumer shopping. Current RESPA regulations have led to a proliferation of charges that makes consumer shopping and the mortgage settlement process both difficult

and confusing, even for the most informed shoppers. Long lists of charges certainly do not highlight the bottom-line costs so consumers can shop and compare mortgage offers among different originators. In addition, under today's rules, the estimated costs on GFEs may be unreliable or incomplete, or both, and final charges at settlement may include significant increases in items that were estimated on the GFE, as well as additional unexpected fees, which can add substantially to the consumer's ultimate closing costs. The process of shopping for a mortgage can also involve complicated financial trade-offs, which are not always clearly explained to borrowers. Today's GFE is not an effective tool for facilitating borrower shopping nor for controlling origination and third-party settlement costs.

The potential for cost reductions in today's market is also indicated by studies showing relatively high and highly variable charges for third-party services, particularly for title and closing services that account for the major portion of third-party fees. There is not enough incentive for loan originators to control settlement costs by negotiating lower costs from third-party providers; rather, they too often simply pass through increases in third-party costs to consumers. Because of their lack of expertise, consumers may not be the best shoppers for third-party services providers, leaving them to rely on recommendations from real estate agents and lenders. Thus, a framework is needed that would encourage competitive negotiations and other arrangements that would lead to lower third-party settlement prices.

Today's mortgage market is increasingly characterized by the introduction of efficiency enhancing improvements such as automated underwriting systems and, through competition, these improvements are leading to lower prices for consumers. But

the one area where current RESPA regulations act as a major barrier to competition and lower settlement services is the production and pricing of settlement services. Under current law, average cost pricing (another cost reduction technique) is inhibited by existing RESPA regulations.

The goal of HUD's RESPA reform is to even the playing field. The rule will accomplish this by requiring lenders to provide consumers information that lenders already have in a format that is transparent. One of the major inefficiencies of imperfect information is the costs of acquiring information. RESPA reform will go a long way toward educating consumers. The first page of the new GFE presents a brief summary of the terms of the loan that would warn prospective borrowers of potentially expensive aspects of the loan including loan amount, maximum interest rate, prepayment penalties, and the total estimated settlement charges. The second page provides more detail on the charges for loan origination and other settlement services. The third page provides a trade-off table so that consumers will learn the relationship between the interest rate and the yield-spread premium. The third page also includes a table so that the consumer can take notes on alternative loan offers and thus comparison shop. Tolerances will limit how much settlement charges can vary once the GFE has been made and the comparison page of the HUD-1 will serve to double-check the GFE regarding settlement charges and provide a summary of the key terms of the borrower's loan at settlement. The final rule also allows settlement service providers to use pricing based on average charges, making their business operations simpler and less costly. It is expected that the new GFE will encourage shopping, increase efficiency, lower housing costs, and promote the purchase of loans that are more suited to a households' needs.

Empirical Evidence of Price Discrimination

Studies indicate that consumers are often charged relatively high fees and can face wide variations in settlement prices, both for origination and third-party settlement services. Chapter 2 offers convincing evidence that not only do borrowers find it difficult to comparison shop in today's mortgage market, but that they are all too often charged excessive prices. The enormous potential for cost reductions in today's market is indicated by studies showing that yield spread premiums do not always offset consumers' origination costs. Studies show that consumers are, in effect, charged relatively high prices in some transactions involving yield-spread premiums, and that the mortgage market is characterized by "price dispersion." In other words, some borrowers get market price deals, but other borrowers do not. Studies show that less informed and unsuspecting borrowers are particularly vulnerable in this market. But given the fact that a borrower may be more interested in the main transaction (the home purchase), even more sophisticated borrowers may not shop aggressively for the mortgage or may not monitor the lending transaction very closely.

The Urban Institute (2008) collected data on 7,560 FHA loans. The mean total loan closing cost for all loans is $4,917 for an average loan amount of $108,237. Total charges are composed of loan charges $3,081, title charges $1,329, and other third party charges $507. It is apparent from the distribution presented below that there is significant variation in closing costs: the standard deviation is $2,381. For its statistical analysis, the Urban Institute focused on a subsample of 6,366 non-subsidized loans, for which the mean total charges are slightly higher at $5,245. Lender charges for non-subsidized loans are $3,390, of which $1,450 are direct fees and $1,940 is the average YSP.

Table 6-5. Distribution of Categories of Closing Costs as a Percentage of Loan Amount (calculated by HUD from data provided by Urban Institute)

Series	5th percentile	25th percentile	50th percentile (median)	75th percentile	95th percentile
Total Closing Cost	2.9%	4.1%	5.1%	6.4%	8.9%
Total Loan Charges	1.3%	2.4%	3.2%	4.2%	6.2%
Yield-spread premium	0.3%	1.3%	2.0%	2.7%	3.8%
Direct loan fees	0.0%	0.8	1.3%	1.8%	3.3%
Total Title Charges	0.6%	0.9	1.2%	1.6%	2.3%
Other Third-Party Charges	0.2%	0.4%	0.6%	0.8%	1.4%

A great degree of variation appears in the lender fees. Since total loan charges are correlated with loan amount, it would be useful to examine the distribution of closing costs as a percentage of loan amounts to ascertain whether the variation in fees is still present. HUD calculated the distributed of these ratios for non-subsidized loans from a data set of closing cost provided by the Urban Institute. There is slightly less variation when measured as a percentage but it is still substantial: the ratio of what the 75th percentile pays as a percentage of the loan to what the 25th percentile pays is 1.8 for total loan charges, 2.1 for the yield spread premium (indirect loan fee), and 2.4 for direct loan fees.

It is apparent that half of the borrowers pay loan charges equal or greater than 3.2% of their loan amount; one-quarter pay loan charges of at least 4.2% of their loan amount; and five percent pay loan charges of at least 6.2% of their loan amount. The

variation is similar for title charges and other third-party charges. Half of the borrowers pay total closing costs equal or greater than 5.1% of their loan; one-quarter pay closing costs of at least 6.4% of their loan amount, and five percent pay closing costs of at least 8.9% of their loan amount.

HUD believes that these data provides strong indications of large price dispersion and thus price discrimination. Price discrimination will always lead to a loss in consumer surplus and unless price discrimination is perfect, it will also lead to a loss in social welfare. It should also be noted that if the variation of fees and charges paid is greater than the actual costs of providing the services, then that constitutes evidence of a violation of RESPA, which explicitly prohibits mark-ups.

First, in a competitive market the price of the good should depend on its quality and not to whom and how it is sold. If there is dispersion because the negotiations are face-to-face, this would suggest that the nature of the market exacerbates the consumer's informational disadvantage. Indeed, there is strong evidence that individuals pay different prices for reasons other than how costly service provisions will be. The Urban Institute report (2008) finds that African Americans pay an additional $415 for their loans and that Latinos pay an additional $365 (after taking into account borrower differences such as credit score and loan amount). These loans are not subprime loans but standard FHA loans. Other researchers have found similar results: Jackson and Berry (2002, see the Regulatory Impact Analysis for reference) find that mortgage brokers charge African-Americans (by $474) and Hispanics (by $580) substantially more for settlement services than other borrowers. Discrimination by race or ethnicity is not economically efficient and would not survive in a perfectly competitive market.

Second, reconsider the yield-spread premium. We mentioned that this is one of the elements of a mortgage that a consumer is not likely to understand. The yield-spread premium is compensation to the broker for selling a loan with a higher interest rate. Thus, as the interest rate rises so should the yield-spread premium. This relationship appears to hold in the data analyzed. The broker earns income from two sources: a yield-spread premium that is paid by the lender and fees that are paid by the consumer. However, the burden of the yield-spread premium is on the consumer, who pays a higher interest rate for loans with a higher yield-spread premium. If consumers were perfectly informed, there would be a negative one-to-one relationship between up-front fees and the yield-spread premium. They simply represent two different ways of compensating the broker for the effort required to originate a loan.

The Urban Institute (2008) finds no strong trade-off between the yield-spread premium and upfront cash payments. Ideally, each dollar of YSP generated by a higher interest rate would result in a one dollar reduction in upfront fees. The reality is that this is not even close to being true. The Urban Institute finds that paying one dollar of YSP to a mortgage broker reduces upfront fees by only 7 cents.[21]

This result is derived from a sample of nonsubsidized loans above with a rate above 7 percent, which is appropriate for investigating YSPs. FHA borrowers appear to get no benefit from YSPSs on brokered loans with coupon rates above 7 percent. The result is not much better when using the larger data set of all nonsubsidized loans:

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[21] In a sample, which is appropriate for investigating YSPs, of nonsubsidized loans with a rate above 7 percent, the Urban Institute finds that broker loan-origination fees, instead of being lower by a dollar for each dollar of YSP, are *higher* by 16 cents. This result is stunningly bad for borrowers. FHA borrowers appear to get no benefit from YSPSs on brokered loans with coupon rates above 7 percent.

The Urban Institute finds that broker loan-origination fees, instead of being lower by a dollar for each dollar of YSP, are higher by 16 cents. This result is stunningly bad for borrowers. Clearly, the average FHA borrower has no idea a higher interest rate can be used to reduce upfront charges. Such a relationship is contrary to what one would expect in a market where there were only minor imperfections. Further evidence is from Jackson and Berry (2002) who studies only brokered transactions, a description of which can be found in Section IV.D.2 of Chapter 2 of the Regulatory Impact Analysis. They find that the problem of price dispersion occurs when yield spread premiums are present, because in these situations there is no single price for broker services: "Most borrowers pay more than 1.5 percent of loan value; more than a third pay more than 2.0 percent of loan value; roughly ten percent pay more than 3.5 percent of loan value." Jackson and Berry find this "price dispersion" troubling, as it suggests that brokers use yield spread premiums as a device "to extract unnecessary and excessive payments from unsuspecting borrowers" (page 9).

Third, consider the confusion that the variety of loan products and permutations of those products can create. If informational asymmetries are significant, then lenders will be able to earn more when selling more complex products. Borrowers who simplify their mortgage shopping by rolling all lender/broker fees into the interest rate (i.e., get "zero-cost" loans) pay $1,200 less for their loans than brokers who pay lender or broker fees as measured by implicit YSPs. Borrowers who pay points realize only $20 of benefits for every $100 of points paid, for a net loss of $80. It appears that the industry is able to take advantage of loan complexity, which is evidence of price discrimination not related to the cost of originating the loan.

Fourth, consider other settlement charges. Title insurance is an industry with a strong potential for natural monopoly. The costs of title insurance are primarily related to research of property transactions. There is a large fixed cost of entry which is compiling a database of transaction and lending records. There should not be a great variation in settlement charges since the only component that does vary substantially is the insurance premium. The Urban Institute (2008) finds an average $1,329 title charge in their sample of all loans with a standard deviation of $564. They also find a significant variation by state with New York, Texas, California, and New Jersey all costing at least $1,000 more (holding property values constant) than North Carolina, the lowest-cost state. A reasonable question is what extra benefits people in the high-cost states get relative to those in low cost states, or why costs are so high if there are no extra benefits. It is also useful to analyze total title costs on a state-by-state basis due to the different legal requirements that exist among the states and the different customs that might have evolved in them as well. HUD examined within state variation of settlement fees. One measure of variability that we calculated for each state was the difference between the median of the highest quartile of title charges and the median of the lowest quartile. This is a measure of the difference between the typical charge for the highest fourth of the borrowers and the lowest fourth of the borrowers within each state. This difference was over $1,000 for nine states. Due to the extent of price dispersion, we can expect significant savings from the final rule.

The primary purpose of this discussion was to show that there is great variation in closing costs and thus room for price discrimination. HUD would like to emphasize that the goal was not to portray lenders, and especially mortgage brokers, as unscrupulous and

harmful to economic welfare. On the contrary, HUD recognizes that mortgage brokers and other lenders have played a crucial role in recent trends in home ownership. It is also clear from the statistical evidence presented in this section that there are many ethical loan originators. One quarter of the borrowers in this sample paid no more than 2.4% in loan charges and 4.1% in total closing costs. Consider that if the entire market mirrored this more efficient segment, then RESPA reform would not be as urgent.

Issues Raised in Comments on the 2008 Initial Regulatory Flexibility Analysis

Section IV.A presents a review of comments on the 2008 IRFA. Sections IV.B and IV.C serve as roadmaps to other issues regarding the rule.

Comments Concerning the Initial Regulatory Flexibility Analysis

This section describes how HUD responded in this Final Regulatory Flexibility Analysis (FRFA) to comments received on the Initial Regulatory Flexibility Analysis of the 2008 proposed rule. The primary comments on the 2008 IRFA included: a report from the National Association of Realtors, prepared by Ann Schnare, who claimed that HUD had underestimated the costs of the rule; criticisms from advocates of small business that HUD had not adequately analyzed the impacts of its rule on industry structure; and an assertion by Representative Manzullo that HUD used obsolete data in its analysis.

"HUD Underestimated the Compliance Costs" (National of Association of Realtors)

Ann Schnare prepared alternative estimates[22] for the National Association of Realtors (NAR) of the compliance costs of HUD's 2008 proposed reform of the Real Estate Settlement Procedures Act (RESPA) to simplify the process and reduce the costs of

[22] Ann E. Schnare, "The Estimated Costs of HUD's Proposed RESPA Regulations," prepared for the National Association of Realtors s (June 3, 2008).

obtaining a mortgage loan. Their report contains worthwhile suggestions, such as performing a sensitivity analysis with respect to the number of applications per loan. However, their cost estimates are inaccurate. In Sections IV, HUD discusses the NAR's major comments that are applicable to the Regulatory Impact Analysis of the final rule. Below is a summary of the NAR's comments and HUD's responses.

The NAR states that HUD ignored a major compliance cost of the rule incurred by loan originators: the hedging costs of guaranteeing the interest rate for the shopping period of ten days. Including hedging costs dramatically increases compliance costs by a factor of four. However, the NAR made an erroneous assumption about the proposed GFE: there is no requirement of an interest-rate guarantee. Thus, hedging costs will be zero (See Section VII.D.1.).

A second criticism of the analysis of the compliance cost of the GFE is that HUD does not consider the possibility that the rule could increase the administrative costs to loan originators by generating a greater demand for GFEs. Although HUD believes that it is just as likely that applications do not increase, HUD has included a sensitivity analysis of compliance costs by the number of applications. (See Section VII.D.2.)

The NAR points to another cost not included in the IRFA: the cost of preliminary underwriting. However, this would only be a factor if the application to loan ratio were to increase. HUD assumed in the IRFA that this ratio would be constant. HUD's response was to include this cost in a high application-to-loan scenario. (See Section VII.D.3)

HUD was criticized for using inconsistent estimates of the value of time in order to raise the value of the benefits of the rule relative to the costs. In fact, the reverse is

true: HUD used a higher rate to estimate the costs and a lower one to estimate the benefits (See Section VII.D.4).

The NAR questions the potential benefits of the GFE. For support, Schnare turned to a study that used a sample suffering from selection bias (See Section V.A.1.g of Chapter 2 for a description) and questioned whether the rule would solve the problem of "bait and switch" or any other misleading business practice. PD&R has recently received A Study of Closing Costs for FHA Mortgages (summarized above in Section III and at length in Chapter 2). The results strongly indicate that HUD's RESPA reform efforts are aimed directly at very serious problems in the market for these loan origination and other settlement services.

Impact of the Rule on Industry Structure

Many industry commenters stated that there were elements of the rule that disadvantaged small business. One of the primary concerns of small title firms is the potential adverse effect of volume discounting. The 2008 final rule set a clearer standard for compliance in the context of the new GFE. HUD merely clarified that volume discounting is legal as long as the savings are passed along to the consumer. ALTA, ICBA, NAMB, and NAR contend that volume discounts will favor large settlement service providers and loan originators/lenders at the expense of small businesses and place them at a disadvantage. The Office of Advocacy formally endorsed this position in their comment letter (June 11, 2008) and predicted that HUD's proposed clarification "may cause small businesses to leave the market and result in higher prices for consumers in the long term."

ALTA stated that the ability to negotiate volume discounts on the local services that are incidental to the issuance of a title policy (such as a title search) will disadvantage the small title insurance agency that does not have the resources to guaranty a stream of business to a third party or discount its own services when the services are performed in house. In addition, ALTA expressed concern that mortgage lenders and brokers will add to the anticompetitive effects by favoring affiliated title companies or those companies that can provide title related services on a nationwide basis.

Comment. Both the NAR and ALTA asserted that the Regulatory Impact Analysis of the proposed rule did not adequately address the anti-competitive issues of the proposed rule.

Response. In its Regulatory Impact Analysis, HUD very meticulously outlined the proportional impacts of the rule on small business. HUD continues to believe that as long as a small businesses is not charging consumers excessive fees, then small business will not suffer disproportionately.

To a large extent, the issue of unfavorable impacts on small business is mute. The greatest objection by small business was to volume discounts. In response to the numerous objections to HUD's clarification, HUD will not address volume discounts in the rule. HUD wants to ensure that any change will adequately protect consumers while at the same time providing adequate flexibility and due consideration to small business concerns. It remains HUD's position, however, that discounts negotiated between loan originators and other settlement service providers, or by an individual settlement service provider on behalf of a borrower, where the discount is ultimately passed on to the borrower, is not, depending upon the specific circumstances of a particular transaction, a

violation of section 8 of RESPA. If the borrower fully benefits from the discount, these types of mechanisms that lower consumer costs are within RESPA's principal purposes.

There may be other facets of the rule, such as tolerances, that are thought to have a disproportionate impact on small business, even on those small firms that are not charging excessive prices. Instead, HUD believes that the rule will create opportunities for efficient firms to expand their operations. This opinion is based on our observations that a distinguishing characteristic of the real estate industry is that it is very locally oriented. The value of proximity and local expertise make small firms more efficient in providing services to consumers. RESPA reform will not change that essential characteristic of the real estate industry. (See Section II.C.5. for a discussion).

Timeliness of Data

Comment. Some criticized HUD for using "old" data in its Regulatory Impact Analysis of the 2008 proposed rule. For example, Representative Don Manzullo wrote in his comment letter that the market has changed significantly since the data was obtained in 2002 and 2004; that these changes may impact how the rule is implemented; and that should wait until it has data on current market conditions before moving forward with the rule.

Response. HUD's initial regulatory flexibility analysis of the proposed RESPA rule, which was completed in late 2007, used the latest, at that time, officially available federal government data on small businesses provided by the Small Business Administration (SBA) as derived from two Census Bureau data sources: the 2002 Economic Census (business income or receipts), and the 2004 County Business Patterns data (number of businesses and firm employment size). These data are augmented, when

possible, by highly regarded data from industry sources. For example, the SBA/Census data on mortgage brokers do not agree with estimates of the size of that industry made by the National Association of Mortgage Brokers and other observers. HUD ultimately based its analysis of the mortgage broker industry on these private sector data.

Chapter 5 of the RIA provides extensive documentation of the characteristics of the industries directly affected by the rule, including various estimates of the numbers of small entities, reasons why various data elements are not reliable or unavailable, and descriptions of methodologies used to estimate (if possible) necessary data elements that were not readily available. The industries discussed in Chapter 5 of the RIA included the following (with Chapter 5 section reference): mortgage brokers (Section II); lenders including commercial banks, thrifts, mortgage banks, credit unions (Section III); settlement and title services including direct title insurance carriers, title agents, escrow firms, and lawyers (Section IV); and other third-party settlement providers including appraisers, surveyors, pest inspectors, and credit bureaus (Section V); and real estate agents (Section VI).

The SBA does not expect to have an update (from the 2007 Economic Census) of the 2002 Economic Census data (business income or receipts) available until sometime in 2010, well beyond the time horizon for this rulemaking effort. Thus, the FRFA of the final RESPA rule will continue to rely in part on data from 2002.

More importantly, HUD's estimate of the annual regulatory burden depends primarily on our assumptions concerning the compliance cost per loan. HUD has used generous estimates of the costs of the rule but has received no hard data from industry that would allow us to refine our estimates. The aggregate impact of the rule depends on

mortgage volume. Our approximation of the average year is 12.5 million transactions. It is probable that the level of originations in 2008-2009 will be lower than this amount. However, the final rule requires a twelve-month implementation period. By the time the rule is in effect, the average mortgage volume is expected to return to that of the average year.

Alternatives Considered to Minimize Impact on Small Businesses

Section VI of this chapter provides discussion of the alternatives considered by HUD in developing the final rule with a focus on those alternatives considered to minimize the impact on small business. Section VI includes a summary discussion of the following major alternatives: maintaining the status quo; not including the yield-spread premium calculation in the GFE; requiring the preparation and reading of a closing script; and clarification in the rule of the legality of volume discounting;. Section VI also includes a discussion of steps HUD took to make the new GFE easier to implement for small businesses.

Comments and Responses to Other Issues

Chapters 1-5 of the Regulatory Impact Analysis include detailed summaries of the comments submitted by small businesses and other firms on various aspects of the 2008 proposed rule and in response to the 2008 IRFA. Detailed discussion of comments received can be found in the preamble. Detailed analysis responding to comments received can be found in Sections VI and VIII of Chapter 3. Detailed discussion of comments related to the compliance burden of the rule can be found in Sections VII, VIII, and IX of this chapter. Analysis responding to some specific comments on the 2008

IRFA can be found in Chapter 3. Changes made to the 2008 proposed rule in response to comments received are summarized in Section VI of this chapter.

Description and Estimate of the Number of Small Entities

Chapter 5 provides extensive documentation of the characteristics of the industries affected by the rule, including estimates of the numbers of small entities. The industries discussed in Chapter 5 included the following (with industry code and Chapter V section reference): mortgage brokers (Section II); lenders including commercial banks, thrifts, mortgage banks, credit unions (Section III); settlement and title services including direct title insurance carriers, title agents, escrow firms, and lawyers (Section IV); and other third-party settlement providers including appraisers, surveyors, pest inspectors, and credit bureaus (Section V); and real estate agents (Section VI). The specific industry names and industry codes (North American Industry Classification System, or NAICS code) for the mortgage originators and third-party firms covered in Chapter V are as follows:

Mortgage Origination Firms

1. Mortgage Loan Brokers (522310)
2. Commercial Banks (522110)
3. Savings Institutions (522120)
4. Real Estate Credit/Mortgage Bankers (522292)
5. Credit Unions (522130)

Third-Party Service Firms

1. Direct Title Insurance Carriers (524127)
2. Title Abstract and Settlement Offices (541191)
3. Offices of Lawyers (541110)
4. Other Activities Related to Real Estate (531390)
5. Offices of Real Estate Appraisers (531320)
6. Surveying and Mapping (except geophysical) Services (541370)
7. Credit Bureaus (561450)
8. Exterminating and Pest Control Services (561710)
9. Offices of Real Estate Agents and Brokers (531210)

Chapter 5 supports Chapters 3 and 6 by providing basic mortgage-related data on each industry and by explaining the various methodologies for estimating the share of industry revenue accounted by the different component industries and by small businesses within each component industry. Chapter 5 presents an overview of the industries involved in the origination and settlement of mortgage loans (see above list). Industry trends are briefly summarized and special issues related to RESPA are noted. There is also a description of the economic statistics for each industry, with an emphasis on each industry's share of small business activity. Both the estimation of the revenue share for various industry sub-sectors (e.g., large title insurers' share of total revenue in the title and settlement industry) and the estimation of the small business share of mortgage-related revenue within the industry, often involve several technical analyses

that pull together data from a variety of sources, in addition to Census Bureau data. This leads to several sensitivity analyses to show the effects of alternative estimation methods and assumptions. This chapter also reports the revenue transfers from the RESPA rule for the specific industry sectors; these transfers are reported in dollar terms and, where possible, as a percentage of industry revenue. Finally, a number of technical issues and special topics, such as techniques for estimating the distribution of retail mortgage originations, are discussed. A technical appendix to Chapter 5 provides relevant definitions and explains the methodology associated with the economic data obtained from the Census Bureau. A data appendix in Chapter 5 includes tables with the economic data (number of firms, employment, revenue, etc.) for each industry sector.

Thus, the Regulatory Impact Analysis pulls together substantial data from the Bureau of the Census and industry sources to provide estimates of revenue transfers for different industries and for small businesses within those industries. Chapter 5 provides a full technical review of the data used and the various methodologies for estimating the small business share of industry revenues.

Drawing from the analysis in Chapters 3 and 5, Appendix A to this chapter provides estimates of the revenue impacts from the new GFE. These data are presented in aggregate form ($ million) and on a per firm basis, covering all firms (both employer and non-employer), small firms (small employer firms plus non-employer firms), and very small firms (very small employer firms plus non-employer firms). Separate data for non-employer firms are also provided. In some cases, different projections are provided for some of the more important sensitivity analyses conducted in Chapters 3 and 5. The technical analyses presented in Chapter 5 indicate some uncertainty around some of the

numbers (such as the number of small mortgage banks, the split of revenue among different sectors of the broad title industry, etc.). Readers are referred to the technical discussion in Chapter 5 for various qualifications with the data and for various sensitivity analyses that illustrate the effects on the estimates of alternative assumptions. In addition, Chapter 5 explains the definitions of small and very small being used here.

Alternatives Which Minimize Impact on Small Businesses

Under the Initial Regulatory Flexibility Analysis, HUD must discuss alternatives that minimize the economic impact on small entities consistent with the stated objectives of applicable statutes, including a statement of the factual, policy, and legal reasons for selecting the alternative adopted in the final rule and why each of the other significant alternatives to the rule considered by the agency was rejected. Many of the alternatives that HUD considered and implemented were directed at making the GFE less burdensome for small businesses. These changes are described below. A more detailed discussion of the changes to make the GFE easier to implement for small businesses are provided in Section VIII of Chapter 3. For a discussion of all of the major alternatives considered to the final GFE, see Chapter 4.

This Regulatory Impact Analysis discusses several steps that HUD took that will assist small businesses involved in the mortgage origination and settlement process. Examples include simplifying the new GFE form (fewer numbers, etc.), designing the new GFE form so that there is a level playing field between lenders and brokers, and delaying the phase-out of today's GFE for twelve months. HUD also made numerous other changes that were designed to make the GFE easier to use, particularly for small businesses. These changes are discussed throughout Chapter 3 and summarized in

several places in the Regulatory Impact Analysis. This section will list them again, as it is useful to provide a record of the changes made to the 2008 proposed rule that should make the new GFE easier to implement for small businesses. Considered as a group, these changes are important. While many are designed to address a problem faced by large as well as small lenders, for the most part, they address problems that would place a greater burden on small than large businesses. Examples of the changes that HUD made are the following:

- Volume-based discounts. Small businesses, especially closing attorneys and escrow companies stated that lenders seeking volume discounts would place them at a competitive disadvantage to larger entities and force them out of business. HUD responded by not addressing volume discounts in its final rule.

- Tolerances. Some commented that large lenders would have an easier time meeting tolerances than small businesses by contracting with large third-party settlement-service providers, and thereby placing small settlement service providers at a competitive disadvantage. If exceeding the tolerance was an infrequent and unpredictable event, larger firms may be able to diversify the risk over a larger pool of loans. The final rule provides loan originators with an opportunity to cure any potential violation of the tolerance by reimbursing the borrower any amount by which the tolerances were exceeded. The opportunity to cure will permit loan originators to give an estimate of expected settlement charges in good faith, without subjecting them to harsh penalties if the estimate turns out to be lower than the actual charges at settlement. This change reduces the potential damages of exceeding the tolerances.

Compliance Costs and Regulatory Burden: New GFE

This section focuses on the compliance, regulatory, and other costs associated with implementing the final rule. It examines compliance and regulatory impacts of the new GFE on originators. There are two types of compliance and regulatory costs – one-time start-up costs and recurring costs. Section VII.B discusses start-up costs, noting that HUD has lengthened the phase-in period for the new GFE in order to reduce any implementation burden on the industry, particularly small firms. Section VII.C discusses recurring costs that are related to implementing the new GFE. The simplicity of the new GFE, plus the changes that HUD has made to improve the new GFE, will limit these annual costs, as discussed in Section VII.D. Section VII.E discusses compliance issues related to tolerances on settlement party costs. Finally, Section VII.F outlines efficiencies associated with the new GFE.

Before examining the specific regulatory and compliance costs, Section VII.A reviews the basic data used in estimating these costs. For a similar description of the costs on the settlement industry, see Section 0.

Data Used in Compliance Cost Estimates

The following tables provide a summary of the industry characteristics data used to develop compliance cost estimates for the GFE. Details on the derivation of these data are available in Chapter 5. The compliance costs of the GFE provisions of the rule apply mainly to retail loan originators. While wholesale lenders, for example, are involved in the mortgage origination process, they are not responsible for issuing the GFE – rather the originating lender or broker is responsible for the issuing the GFE to the borrower.[23]

[23] If the wholesale lender generates the GFE, then there would be a charge to the originator (either a direct charge or a reduction in fees, compared with the case where the originator issues the GFE).

Therefore, data are presented only for those brokers and lenders that do retail mortgage loan originations. Settlement agents do not generate GFEs and therefore they would not be subject to these GFE-related costs. Settlement agents will , however, be involved generating HUD-1s; since there are some changes to the HUD-1 form, there are compliance costs on settlement agents associated with that change. In most cases, HUD expects that loan originators will complete the comparison page of the HUD-1 form. However, a portion of the compliance cost will be the burden on settlement agents of completing the comparison page accurately in cases where there is additional information required from the settlement agent. Other third-party providers (e.g., appraisers) will face no compliance costs from the GFE provisions of the rule.

Chapter 5 provides information on the total number of brokers and lenders that are likely to be affected by the new RESPA rule and its revised GFE form. Section II of that chapter explains that the number of brokers has grown substantially in recent years. In 2000, there were 30,000 brokers, but with the increase in refinancing, the number of brokers rose to 33,000 in 2001 and then jumped to 44,000 in 2002 and then to 53,000 in 2004. According to Census Bureau data, practically all brokers (99.1%) qualify as a small business. Thus, it is estimated that small broker firms have ranged from 32,703 to 52,523 over the past few years. As explained in Section III of Chapter 5, lenders that will be affected by the RESPA rule include: 7,402 commercial banks (4,426 or 59.8% are small), 1,279 thrift institutions (641 or 50.1% are small), 1,287 mortgage banks (1,077 or 83.7% are small), and 3,969 credit unions (3,097 or 78.0 % are small).[24] Altogether,

[24] See Section III.B.5 of Chapter 5 for issues related to the number of small mortgage banks. As also explained in that section, the credit unions are the ones that report some mortgage origination activity.

there are 13,937 lenders (including credit unions) affected by the RESPA rule, and 9,241 of these qualify as a small business.

Table 6-6 provides the distribution of retail mortgage originations among the various industries and for small firms within each industry. Totals are estimated based on the number of mortgage originations (12,500,000 loans) that would occur in a "normal" year of mortgage originations (that is, not in a high-volume year with a refinancing boom). The data below assume that brokers account for 60% of mortgage originations and lenders, the remaining 40%.[25] (See below for alternative origination volume and broker share estimates.)

[25] See Section III.B.5.d of Chapter 5 for the derivation of the distribution of retail originations among commercial banks, thrifts, and mortgage banks; the distribution used here is the "adjusted distribution" for the number of loans. See Chapter 5 for reasons why there is some uncertainty with the estimated distribution and for analysis of an alternative distribution.

Table 6-6 Volume of Retail Mortgage Originations

Industry	All Originations	Percent of Originations	Originations by Small Firms	Percent Industry Originations by Small Firms
Mortgage Brokers	7,500,000	60.00%	5,250,000	70.00%
Commercial Banks	2,053,150	16.43%	389,893	18.99%
Thrifts	974,750	7.80%	120,089	12.32%
Mortgage Banks	1,551,500	12.41%	644,803	41.56%
Credit Unions	420,600	3.36%	122,563	29.14%
TOTAL	12,500,000	100.00%	6,527,349	52.22%

As shown in Table 6-6, it is estimated that 52% of mortgages are originated by small brokers and lenders.

Table 6-7 provides the total number of workers and the number of workers in small firms engaged in retail mortgage origination by industry. It is based on the mortgage origination volumes depicted in Table 6-6 and productivity rates of 20 loans per worker per year for mortgage brokers and lenders. See Section II.B.2.c of Chapter 5 for the derivation of the 20 loans per worker in the broker industry and see Section III.B.5.g of Chapter 5 for a discussion of the 20 loans per worker in the lender industry. Given the uncertainty around these estimates (and particularly the lender estimate which is obtained by simply assuming that lender workers are as productive as brokers), alternative estimates and sensitivity analyses are provided in Chapter 5. As noted in Chapter 5, one alternative would be to choose a lower productivity number for lenders, which would be consistent with the widely held belief that brokers are more productive

than lenders; in addition, it may be more appropriate to overestimate the number of lender employees affected by the RESPA rule than to underestimate them.[26] However, this analysis starts by assuming equal productivity for lenders and brokers.

Table 6-7 Workers Engaged In Retail Mortgage Loan Origination

Industry	Total Workers	Workers in Small Firms	Percent of Workers in Small Firms
Mortgage Brokers	375,000	288,750	77.00%
Commercial Banks	102,658	19,495	18.99%
Thrifts	48,738	6,004	12.32%
Mortgage Banks	77,575	32,240	41.56%
Credit Unions	21,030	6,128	29.14%
TOTAL	625,000	352,617	56.42%

As shown in Table 6-7, it is estimated there are 625,000 workers engaged in mortgage origination, with 352,617 of these operating in small businesses. As noted above, the mortgage volume figure (12,500,000 loans based on $2.4 trillion in originations) reflects industry projections of mortgage originations for 2008. Chapters 3, 4, and 5 conduct sensitivity analyses with a higher level of originations. For example, one could consider an environment where 15,500,000 loans were originated (compared with the 12,500,000 loans in the base case). In this case, the figures in Tables 6-6 and 6-7 would change. For

[26] A comment should be made about the small business share for brokers. Section II.B.1 in Chapter 5 reports that small brokers account for 70% of broker industry revenue. Table 6-6 assumes that small brokers account for the same percentage (70%) of the number of loans originated by all brokers; it is possible that this percentage could be too low, given that Section II.B.2.c of Chapter 5 derives an estimate of 77% for the share of industry workers in small broker firms. The 77% figure is used in Table 6-7 (288,750 divided by 375,000) for estimating the share of workers in small broker firms. The small business share of the number of workers in each of the four lender industries in Table 6-7 is assumed to be the same as in Table 6-6 for the number of loans. See Section III.B.5 of Chapter 5 for the derivation of the small lender shares of lender originations.

example, the number of workers in the broker industry would increase to 438,038 (with 337,293 in small firms) and the number of workers in the combined lender group would increase to 271,250 (with 69,296 in small firms).[27] Below, sensitivity analyses cover these higher estimates of the number of workers affected by the RESPA rule.

Compliance and Regulatory Burden: One-Time Costs

Several one-time compliance burdens can be identified that will result from the new rule. All involve the adjustment process from the old rule to the new rule. Although HUD received comments on the one-time compliance cost issues associated with the new GFE, commenters did not provide any useful data on the magnitude of these costs. There are three major areas of expected one-time compliance costs of the new GFE. Those who generate the new GFE forms, loan originators, will need new software in order to produce the new forms.[28] Their employees will need to be trained in the use of the new forms and software. Loan originators may seek legal advice to be certain that the arrangements they make to ensure that third-party service prices are accurate and within tolerances comply with the regulation. Loan originators may also seek legal advice regarding tolerances and average-cost pricing. In this section, it is estimated that these one-time compliance costs will total $383 million, although it is recognized below that these costs could vary with several factors such as different levels of overall mortgage

[27] As explained in Chapter 5, this scenario assumes that the increase in mortgage originations comes mainly from brokers; the loans-per-worker assumption is increased to 23 for brokers (consistent with that number increasing in Olson's surveys during higher volume years) but kept at 20 for lenders since their volume does not increase much during this scenario.

[28] This analysis assumes that the mortgage broker, not the wholesale lender, produces the GFE in transactions involving mortgage brokers. To the extent that the wholesale lender is involved in producing the GFE the use of the broker data will result in an overestimation of the impact on small businesses (since small businesses make up a much larger portion of broker businesses than they do of wholesale lender businesses).

activity. Small brokers and small lenders firms will experience $268 million (or 70%) of these one-time compliance costs.

Software Modification and Training Costs

Loan originators would need alterations to their software to accommodate the requirements of the new rule since they generate the new GFE. There would be one-time costs for production and installation of the new GFE (software development, etc.). Software modification, or new software, is needed because the GFE has been changed. The implementation of software varies with business size. Small originators are likely to use commercial off-the-shelf (COTS) software products while larger originators may produce their own software if in-house development is cheaper than buying from outside suppliers. HUD reviewed several software products for loan origination and closing advertised on the Internet.[29] Prices ranged from a flat $69[30] for one license to undisclosed negotiated prices based on the number of users and feature sets purchased. Software is generally priced according to the number of users (e.g., one license per user, or enterprise licenses based on the expected number of users in the enterprise).
One new requirement, implicit from the tolerances, is that originators will have to keep track of the costs listed on the GFE in order to ensure that the tolerances are not exceeded at settlement. Most of the software products HUD examined have the capability to access databases of information, including pricing information, of third-party service providers. Because these systems have the capability to access other databases, they

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[29] Examples are: Vantage ILM, http://www.vantageilm.com; Utopia Originator from Utopia Mortgage Software, http://www.callutopia.com/support.html; The Mortgage OfficeTM from Applied Business Software, http://www.themortgageoffice.com/main.asp; and MORvision Loan Manager from Dynatek, http://www.dynatek.com/products.asp.

[30] Good Faith Settlement Software by Law Firm Software; http://www.lawfirmsoftware.com/software/good-faith-estimate.htm. Note that this is very basic software compared to other alternatives. More sophisticated software is more expensive.

would not need to be redesigned to carry forward prices from the GFE to the closing documents in order to determine if final settlement prices remain within tolerances. The GFE portion of the software would need to be modified to display the consolidated expense categories mandated in the rule. Redesigning the form appears to constitute a minor alteration of the software.

The new GFE also requires additional information. The first page summarizes worst case scenarios for the borrower: the maximum monthly interest rate, the maximum monthly mortgage payment, and maximum loan balance. Such information is obvious for most types of loans but could require more effort to calculate for more exotic loans such as a negative amortizing loan. Some loan origination software will already possess analytical capabilities. However, producers of less sophisticated programs will need to write a few additional lines of code to create the output for the first page of the new GFE. Nonetheless, the final rule will have no impact on the primary function of origination software and would require only minor changes.

Changes to the HUD-1 will have implications for loan origination software. The comparison page, which features a summary of the loan terms, requires lenders to provide information on the loan and settlement costs for pa3 3 of the HUD-1. Indeed, it is possible that most producers of loan origination software will begin to feature an application that generates an almost complete HUD-1 for the settlement agents to finish. One could add this application to loan origination software fairly easily. It will be a minor change since lenders enter most of the information needed for the comparison page for the GFE. The task facing the programmer will be to set up an interface for entry of additional escrow information needed in the comparison page, populate page 3 of the

HUD-1 form with settlement cost and loan term data and print out the HUD-1 form. The software would also perform the important task of calculating the difference between the figures on the initial GFE and the actual settlement costs and then check whether they are within the tolerances.

Depending on the software that a firm has purchased there are three possibilities as to who pays the direct cost of developing new software. The first scenario is that a firm purchases an update of the program. This is a fairly standard option and is generally less than half the price of new software. Given that the changes required by the final rule are fairly minor, the price of an update should compensate software companies for the cost involved in altering their programs.

The second possibility is that a firm purchases new software, in which case the cost of redesigning the forms to comply with the rule will be built into the purchase price. Firms that would purchase new software would include new entrants into the industry, pre-existing firms that would have bought new software for reasons unrelated to the final rule, and firms that use software for which updates are not offered. Many users routinely upgrade software as new versions are released and build the expected expenses into their business plans. To the extent that software is routinely upgraded, the extra costs of implementing the GFE changes will be reduced. In these cases, the software cost to the firm of the final rule is not the purchase price of the software but rather the increase in the purchase price as a result of the costs of redesigning software to meet RESPA guidelines.

A third scenario is that software companies are obliged or volunteer to offer free updates, in which the case the software cost of the final rule falls directly on software developers. However, indirectly, the cost of the new software will be shared by real

estate and software firms. Software companies that offer free updates will price the risk of changes into the purchase price of the software. If a large unexpected change occurs, then the software company will bear the burden. However, the change required by RESPA will not be unexpected because the final rule will be made public and will not be costly for reasons previously discussed.

In all three scenarios, the cost of an update is a good approximation of the software cost of the rule. In the first scenario in which firms purchase an update, it would probably be an overestimate of the cost to a purchaser because an update may contain other useful improvements to the software. However, it is a reasonable estimate of the cost in that many firms would not purchase an update if not for the final rule. In the second scenario, in which a firm purchases new software, the price of an update could serve as an approximation of the cost of implementing the required changes and thus an estimate of the resulting increase in the price of new software. In the third scenario, where the software companies bear the direct cost of the change, the price of an update could serve as an estimate of the cost to software firms of producing free updates.[31]

In the first two scenarios, where firms bear the burden of the change in the software; the costs of new or updated software will depend upon the number of employees in the firm using the software. Virtually all software companies providing software to lenders for loan origination offer volume discounts. Such a pricing policy reduces the average cost for large firms. Second, in larger firms many employees will have specialized duties that do not include completing the new GFE form and so will not

[31] Correctly estimating the cost to software firms is difficult given the nature of the output. Development is a one-time fixed cost, whereas the cost of delivering software to one user is very low. Given the decreasing average costs, the aggregate economic impact to the software industry would depend upon the number of firms.

require updated software. Thus, it is likely that small firms will bear a greater per employee software cost from the final rule.

Based upon the discussion above and an examination of software pricing schemes, it is reasonable to make three assumptions in order to estimate the software costs of the final rule: 1) the cost per user is the cost of an update; 2) updates cost less than half of the cost of new software; 3) the costs per user for a firm decline significantly with the number of users. An example of the type of software that a firm might purchase is Bytepro Standard (by Byte Software, Inc., http://www.bytesoftware.com). This software has many analytical features such as the ability to calculate maximum loan amounts, which would be required by the new GFE. The software costs $395 for a two user package and $400 for five additional users. The per user cost for the first two is $198. The cost per user for an additional five is $80.

We can safely assume that the industry average of the cost of an update would be no more than $150 for the first user, $100 per user for the average small firm, and $50 for the average large firm.[32] Second, we assume that the proportion of workers involved in origination that use the software declines with the size of the firm. For small firms, we assume that three-quarters of all workers use the software and will need an update. For large firms, we assume that only half of the workers use origination software and need an update. Given these assumptions, the total cost to the industry of an update would be $33

[32] Byte Software, Inc. offers an annual support service, which would include updates, for up to ten users for $300 per year. Every additional user over ten cost $30.

million, of which $26 million is borne by small firms.[33] This amounts to an average software update cost of $83 per user.

In addition, each employee using the new software would require some time to adjust to the changes. The actual amount of time required to familiarize ones self with the new software is unknown. For this example it is assumed that 2 hours are required. If the opportunity cost of time is $72.12 per hour (based on a $150,000 fully-loaded annual salary), then the opportunity cost of software training would be $144 per worker using the new software. Software users often learn about new modifications without formal training by using them with very little loss of time or productivity. Thus the software training costs estimated below are likely an upper bound. Table 6-8 shows the distribution of these costs by industry and the amount borne by small businesses within each industry. The table uses worker distributions from Table 6-7 and assumes half of the workers in large firms and three-quarters of the workers in small firms use the software and will require upgrades and training. Given these assumptions the total software training cost is $58 million, of which $38 million is borne by small firms. The grand total for software upgrade and training cost is $91 million, of which $65 million is borne by small firms.

[33] To demonstrate that our estimate is a safe ceiling, suppose that there are one hundred software firms and that each one pays six programmers an average of $150,000 a year to upgrade the software to reflect the changes incurred by the proposed rule. The total cost to the software industry would be $90 million.

Table 6-8 One-time Software Upgrade and Training Costs of the Rule to Loan originators

Industry	Total Software Upgrade and Training Cost	Small Business Cost	Percentage Small
Mortgage Brokers	$61,267,428	$52,891,226	86.3%
Commercial Banks	$11,647,288	$3,570,897	30.7%
Thrifts	$5,249,891	$1,099,855	21.0%
Mortgage Banks	$10,308,241	$5,905,531	57.3%
Credit Unions	$2,569,710	$1,122,511	43.7%
TOTAL	$91,042,558	$64,590,020	70.9%

Alternative estimates could be made. If 4 hours (instead of 2 hours) of software training were required, then total costs would rise by $57 million to $148 million (with $103 million being the small business cost). Assuming that only two hours are required, but that the proportions of software users were raised to all of the workers in small firms and three-quarters of the workers in large firms, then the total software cost (including training) of the final rule would be $126 million, of which $86 million would be borne by small firms. If the proportions are increased (as in the latter scenario) and the hours are increased (as in the former scenario), then the total cost would be $206 (with $137 million being the small business cost).

The estimates in Table 6-8 above are based on a "normal" level of mortgage origination activity and not that of a high volume year which might occur as a result of low interest rates. High volume years bring with them increases in productivity by existing firms and employees (higher rates of loans per employee), new employees, and

new entrants. New employees and new entrants would require additional software licenses even if there were no new rule changing the GFE. For this reason, basing the software upgrade compliance burden on a high volume year would overstate the burden. Using the higher rates of productivity associated with refinancing booms to compute software upgrade costs would tend to understate them. Therefore, use of the normal business volume probably provides the most appropriate estimate of this cost. Still, assuming a higher level of origination activity (15,500,000 loans) and a 65% market share for brokers, estimated software costs would be $118 million, and $86 million would be accounted for by small businesses (with one-half of employees at large firms and three-quarters of workers at small firms using the software and requiring 2 hours of training). As noted earlier, the costs of software upgrades required to implement the new GFE apply only to retail loan originators. These costs do not apply to wholesale lenders.

Another way of presenting the software and training costs to loan originators is to distinguish between the costs of the new GFE versus the HUD-1. This break-out is somewhat arbitrary but is useful for the discussion of the costs of the different components of the rule. Suppose the HUD-1 alterations constitute 20 percent of the software and training costs to loan originators, then of the $91,042,558 total costs to loan originators, $72,834,046 stem from the GFE and $18,208,512 from the HUD-1. The costs to small business would be distributed similarly: $52 million from the GFE and $13 million from the HUD-1. One could experiment with different ratios of HUD-1 to GFE costs but the total would not change.

Legal Consultation

Using the new GFE will entail a change in business practices, including making arrangements with third-party settlement service providers to ensure that prices charged will remain within the tolerances of the prices quoted. Loan originators will want to ensure that these arrangements do not violate RESPA. It is highly likely that the trade associations for the mortgage loan origination industries will produce model agreements or other guidance for members to help them comply with the new rule. Loan originators may also want to better understand if there any legal implications of average-cost pricing. Some originators may feel no further need for additional legal advice so that they would have no legal consultation expenses as a result of the rule. Larger originators may wish to seek a greater amount of legal advice, as they perceive themselves to be at greater risk of class action RESPA litigation.

The actual amount and cost of legal services that will be incurred because of the new GFE are unknown. While it is recognized that all firms might not seek legal advice, it would seem that many firms engaged in retail mortgage origination would want some minimal legal advice, so that they understand the new rules and regulations. If all 57,937 firms sought two hours of legal advice at $200 per hour, the fixed legal consultation expense would amount to $23 million. In addition, firms will seek further legal advice based on their volume of transactions; in this analysis, the total volume-based legal expense amounts to 4 times the fixed expense or $93 million. To show that this is a reasonable estimate, suppose a large originator, operating in all 50 states and the District of Columbia, required state-by-state legal reviews averaging 1-person-week (40 hours) per state. At $200 per hour, this would amount to $408,000. If all of the 100 largest

originators acquired a similar amount of legal advice, the cost would come to $40.8 million, which leaves approximately $52 million for variable legal costs for other originators.[34] Under these estimates, total legal consultation expenses associated with the new GFE are expected to total $116 million and are distributed among industries and small businesses, which bear 60.3% of the legal cost, as depicted in Table 6-9, which uses information on the distribution of firms and originations.

Table 6-9 One-time Legal Consultation Costs of the New GFE

Industry	Total Legal Consultation Cost	Small Business Cost	Percentage Cost to Small Business
Mortgage Brokers	$73,219,520	$56,375,264	77.0%
Commercial Banks	$18,186,829	$4,934,375	27.1%
Thrifts	$7,740,284	$1,182,697	15.3%
Mortgage Banks	$12,020,625	$5,212,708	43.4%
Credit Unions	$4,706,743	$2,147,722	45.6%
TOTAL	$115,874,000	$69,852,767	60.3%

The costs of legal consultation required to implement the new GFE apply only to retail loan originators. Wholesale lenders and settlement agents and other third-party settlement service providers do not provide GFEs and therefore they would not be subject to these costs.

[34] If the per hour cost of legal consultation were greater than $200 per hour, then these estimates would rise proportionately with the increase in hourly legal costs.

Employee Training on the New GFE

Loan originators must fill out the new GFE and be familiar with its requirements so that they can fill out the form correctly and respond to the borrower's questions about it. So, there would be a one-time expense of training loan originators' employees in the requirements of the new rule in a range of issues such as the new forms and average-cost pricing. While the actual extent of the required training is unknown, a reasonable starting point would be that one quarter of the workers in large firms and one half of the workers in small firms would require training concerning the implications of the final rule. We assume that small firms pay tuition of $250 per worker but that large firms receive a discount and pay only $125 per trainee. If the training lasts an entire day, then the opportunity cost of the time, at $72.12 an hour (based on a $150,000 fully-loaded annual salary) would be $577 per trainee. The total tuition cost to the industry would be $53 million and the opportunity cost of lost time would be $141 million, amounting to a total training cost of $194 million. The total one-time cost for RESPA training for originator staff in the new rule would come to $194 million or $310 per worker (averaged across all workers). The one-time cost for small businesses is $146 million. Table 6-10 depicts the distribution of training costs among the retail mortgage origination industries and for small businesses in each industry. It uses data on workers from Table 6-7.[35]

[35] Sensitivity analysis shows the effects of changing the number of workers participating in the training. If one half (rather than one-quarter) of workers at large firms and three-fourths (rather than one-half) of the workers at small firms attended training, then the total costs would be $314 million (with the small business share being $219 million); the average cost per employee would be $503. However, as noted in the text, there may be other, less costly ways in which the knowledge necessary to comply with the GFE provisions of the final rule can be imparted to workers, which will reduce the number of workers that need formal training.

Table 6-10 One-time Worker Training Costs of the New GFE

Industry	Total Training Cost	Small Business Cost	Percentage Small Business Cost
Mortgage Brokers	$134,522,236	$119,387,019	88.7%
Commercial banks	$22,653,771	$8,060,292	35.6%
Thrifts	$9,981,440	$2,482,613	24.9%
Mortgage Banks	$21,285,461	$13,330,070	62.6%
Credit Unions	$5,148,741	$2,533,751	49.2%
TOTAL	$193,591,648	$145,793,746	75.3%

As explained earlier, the costs of training are probably best estimated using the more normal mortgage environment, since many of the additional employees during a refinance wave are temporary employees who may either do only general office work that does not require any GFE-specific training or who may be trained on-the-job by existing permanent employees. Still, the higher figures are reported for those who believe they are the relevant figures.

The data and table presented above depict what is likely to be an upper bound for training costs. There are other, less costly ways in which the knowledge necessary to comply with the provisions of the final RESPA rule can be imparted to workers. Small firms, in particular, are likely to take advantage of information on complying with the final rule provided by trade associations and their business partners (such as wholesale lenders), and these firms may find the time and expense of formal training unnecessary. To the extent that this is the case, the estimates reported above will over state the impact on small businesses.

We assume that no training specific to the HUD-1 will be required. Any training in the rule concerning the GFE will cover the HUD-1 as well for the loan origination industry. Almost all of the information required for the HUD-1 is from the GFE. Training concerning tolerances is a GFE issue, even though the calculation is presented on the HUD-1.

Comments Concerning One-Time Adjustment Costs

Comments. Lenders and their trade associations opposed a 12-month implementation period on the basis that 12 months is insufficient time to prepare for compliance with the new requirements. According to one major lender, a 12-month period is far too short given the extensive nature of the changes. This lender estimated that an 18-24 month period will be required for implementation of the proposal as published on March 14, 2008. According to other major lenders, the proposed rule would require significant systems and operational changes well beyond the complex forms changes, and would take a minimum of two years to implement.

Response. HUD has determined to adopt a 12-month implementation period. HUD recognizes that operational changes will be required in order to implement the new rule, in addition to training staff on the new requirements. However, the need for a standardized GFE with relevant information about the loan and settlement charges is critical in light of the problems in the current market and further delay is not warranted. HUD believes that a 12-month implementation period will provide sufficient time for systems changes and training to occur. In order to ensure a level playing field, during the transition period, settlement service providers will be required to comply with the current

RESPA requirements. The requirements set forth in the rule will apply to all settlement service providers 12 months after the effective date of the rule.

Compliance and Regulatory Burden: Recurring Costs of the GFE

This section discusses recurring costs associated with the new GFE. Several topics are addressed, some of which have already been discussed in previous sections. We expect that the new GFE will probably be neutral (see the conclusion of Section 0) but that it may impose a burden of ten minutes per application. Assuming that to be the case and that the ratio of applications per loan remain at 1.7, then the annual recurring compliance cost of the GFE from completing applications would be $20.40 per loan, $255 million on all firms, of which $134 is borne by small business. If the loan to application ratio increases to 2.7, then the annual recurring compliance cost of completing applications will be $32.40 per loan, $405 million in total, of which $213 million is imposed on small business (see Table 6-11 below and section VII.D.2). Costs of the additional time spent to arrange the pricing that protects the originator from the costs of the tolerances being exceeded is estimated to be $12 per loan or $150 million annually, of which $79 million is paid by small business. This additional cost of arranging tolerances does not vary by the number of applications per loan.

Table 6-11 Recurring Compliance Costs of the New GFE by the Number of Application per Loan

	Per Loan Cost		Total Cost: All Firms (Millions)		Total Cost: Small Firms (Millions)	
Source of Additional Cost	1.7	2.7	1.7	2.7	1.7	2.7
Processing Applications	$20.40	$32.40	$255	$405	$134	$213
Arranging Tolerances	$12.00	$12.00	$150	$150	$79	$79
Initial Underwriting	$0.00	$11.00	$0	$138	$0	$72
Total Cost of GFE	$32.40	$55.40	$405	$693	$213	$364

A third source of recurring compliance costs is that of underwriting additional applications. If there is no change in the application per loan ratio as a result of the rule, then the compliance costs of underwriting additional applications will be zero. If the application per loan ratio increases to 2.7, then the recurring compliance cost from preliminary underwriting will be $11 per loan, $138 million across all firms, of which $72 million is from small business (see Section VI.D.3). The total recurring compliance cost on loan originators of the rule at 1.7 applications per loan is estimated to be $32.40 per loan or a total of $405 million ($213 million from small business). At 2.7 applications per loan, the annual recurring compliance cost of the GFE is $55.40 per loan or a total of $693 million ($364 million from small business).

Cost of Implementing the New GFE Form

This section examines the various costs associated with filling out and processing the new GFE. In their comments on the 2008 proposed rule, loan originators commented that the proposed GFE was longer than today's GFE and that it would take more time to

fill out. In addition to settlement charges, the proposed GFE contained loan terms, a trade-off table, a breakout of lender and broker fees, and a breakout of title agent and insurance fees.

There are several aspects of the new GFE that must be considered when estimating the overall additional costs of implementing it. The following discusses the various factors that will reduce costs and possibly add costs to the GFE process. As is made clear by the discussion, there should not be much, if any, additional cost with implementing the new GFE (as compared with implementing today's GFE).

(1) Disclosure of YSP. Under the existing scheme, mortgage brokers are required to report yield spread premiums as "paid outside of closing" (POC) on today's GFE and HUD-1. Page 2 of the new GFE has a separate block for yield spread premiums (as well as for discount points). In order to fill out a GFE under the final rule, the mortgage broker must have a loan in mind for which the borrower qualifies from the information available to the originator. Pricing information is readily available to mortgage brokers, so there is no additional cost incurred in determining the yield spread premium or discount points since they have to look and see if there is a yield spread premium under the current regime anyway. Since it is reasonable to assume that all brokers consult their rate sheets prior to making offers to borrowers, it is reasonable to assume that they know the difference between the wholesale price and par. It does not appear that disclosing the yield spread premium or discount points adds any new burden.

(2) Itemization of Fees. The reduction in the itemization of fees will lead to fewer unrecognizable terms on the new GFE.[36] That should lead to fewer questions about them and less time spent answering those questions. Of course, to the extent that the originator is precluded from including junk fees on the GFE, he or she will not have to spend any time trying to explain what they are. The confusion avoided may lead the borrower to better understand what is being presented so that questions on useful topics are more likely to come up and the originator can spend his time giving useful answers (or more time will be spent explaining useful things). In all, the simpler GFE produces a savings in time for originators and borrowers.[37]

(3) Summary Page. A summary page has been added to the new GFE in the final rule. But it should be noted that the summary page of the new GFE asks for basic information (e.g., note rate, loan amount) that is readily available to the originator and thus do not involve additional costs. The summary page simply moves items around or repeats items rather than requiring new work.

(4) Trade-Off Table. There is a burden to producing and explaining the worksheet in Section IV (on page 3 of the GFE) showing the alternative interest rate and upfront fee combinations (the so-called "trade-off" table or worksheet). Many commenters said customizing the trade-off table with the individual applicant's actual loan information would be difficult; these commenters recommended a generic example, possibly placing it in the HUD Settlement Booklet, rather than providing it with the GFE.

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[36] The fees in the lender-required and selected services section will still be itemized (e.g., appraisal, credit report, flood certificate, or tax service) as will those in the lender-required and borrower selected section (e.g., survey or pest inspection). There will, however, be no itemization or long lists of various sub-tasks of lender fees or title fees, often referred to as junk fees.

[37] Several items were dropped from the new GFE, as compared with the proposed GFE: the APR, the breakout of the origination fee into its broker and lender components, and the breakout of the title services fee were dropped. These were considered unnecessary for comparison shopping.

However, it is important to remember that the information in the worksheet is likely to be a reflection of a worksheet the originator already uses to explain the interest rate/upfront fee trade-off. While there may be a burden to explaining how the interest rate-point trade-off works, this explanation is something all conscientious originators are already doing in the origination process. In today's market, most lenders and brokers likely go over alternative interest-rate-point combinations with potential borrowers. For these originators, there is no additional explanation burden arising from the production of this worksheet. To the extent that some lenders only explain one option to a particular borrower (even though they offer others), there would be some additional costs for those lenders. Today, most originators present to borrowers much more complicated sets of alternative products than captured by the worksheet. It is important to remember that the main purpose of the worksheet is simply to sensitize the borrower to the fact that alternative combinations of interest rates and closing costs are available.

With respect to customizing the worksheet to the applicant's actual offer, the information on the applicant's loan is already on the new GFE, so that would not appear to be a significant problem, as that applicant information can be linked directly into the worksheet. Then, there is the issue of the two alternative combinations, one with a lower interest rate and one with a higher interest rate. Most originators offer loans with several interest rate and point combinations from which the borrower chooses. As noted above, they probably have already discussed these alternative combinations with the applicant. The originator would pick two alternatives from among the options available but not chosen by the borrower when he picked the interest rate and point combination for which his GFE is filled out. The originator would have to punch these other two combinations

into his GFE software (two interest rate and point combinations) in order for the software to fill out the form. In the event that the originator does not use software to make these calculations, they would have to be done by hand.

(5) Documentation Costs. Loan originators are required to document the reasons for changes in any GFE when a borrower is rejected or when there are changed circumstances that result in cost increases. Once a GFE has been given, there are several potential outcomes. One is that the loan goes through to closing with tolerances and other requirements met. Another is the borrower terminates the application. Borrowers could also request changes, such as an increase in the loan amount. There could also be a rejection, a counteroffer, or unforeseen circumstances.

The March 2008 proposed rule provided that a borrower could be rejected at the GFE application stage if the loan originator determined that the borrower was not credit worthy. The borrower could not be rejected at the mortgage application stage unless the originator determined there was a change in the borrower's eligibility based on final underwriting, as compared to information developed for such application prior to the time the borrower chose the particular originator. Under the proposed rule, the originator would have been required to document the basis for such a determination and maintain the records for no less than three years after settlement.

One lender commented that under HUD's March 2008 proposed rule, lenders would be required to retain the GFE application for three years which is different from the 25 month retention requirement by TILA or ECOA. The lender commented that this difference presents additional expense without a substantive benefit to the consumer.

The first two require no special treatment. Borrower requested changes do not require documentation but do require a new GFE, as explained in (5) above. The case of borrower rejection (which assumes there is no counteroffer accepted by the borrower) requires documentation today under the Equal Credit Opportunity Act (ECOA). Under ECOA, the originator must document the reason for a rejection and retain the records for 25 months, which is also the requirement in the final rule. Therefore, there is no additional documentation required in case of a rejection. There is no documentation requirement for a counteroffer, but the lender must issue a new GFE to the borrower; the minimal burden associated with issuing an additional GFE.

Documentation for changed circumstances adds a new requirement. The additional burden associated with changed circumstances comes from having to document the reasons for the increase in costs and from determining that the amounts of the increases in charges to the borrower are no more than the increases in costs incurred by the changed circumstances. The Department does not require that a justification document be prepared. Since there are no special reporting requirements when changed circumstances occur, compliance could be met by simply retaining the documentation in a case binder, as any other relevant loan information might be retained in a case binder today. For example, itemized receipts for the increased charges would simply be put in the loan case binder (as they probably are today). Case binders are stored now. The additional cost of identifying and storing the documentation in that binder would be de minimus. This would represent little burden on the originator, particularly since unforeseen circumstances will not be the norm.

There may be some record retention issues with small originators, such as brokers. If small originators retain case binders today, then their situation would be similar to other originators. If they do not retain the case binder today, then they may choose to do so, or they may rely on their wholesalers for record retention. It might well become a selling point for wholesalers. Relative costs of storage, reliability, and accessibility would determine who could best perform this function.

(6) Crosswalk from New GFE to New HUD-1. The HUD-1 in the final rule has been changed so that it matches up with the categories on the new GFE – making it simple for the borrower to compare his or her new GFE with the final HUD-1 at closing. In addition, a comparison page has been added to the HUD-1 to clarify any changes in settlement fees. The simplification of the GFE does not add any burden for the borrower to the comparison of the figures on the two forms – rather it will be reduced since it will now be easier for the borrower to match the numbers from the GFE (issued at time of shopping) with those on the HUD-1 (issued at closing). Compared with today, it also eliminates the step of adding a pointless list of component originator charges to get the relevant figure, the total origination charge. In addition, the elimination of extra itemized fees on the GFE may lead to the elimination of them on the HUD-1 since they may have been on the GFE only to overwhelm the comparison shopper. Even without the new comparison page, the settlement would have been more transparent for the borrower. However, requiring that an additional page be completed will impose some costs on the industry. Compliance costs of the this change are discussed in detail below.

(7) Mortgage Comparison Chart ("Shopping Chart"). The shopping chart is on the third page of the GFE. It is delivered to the borrower as a blank form. The borrower is

free to fill it out and use it to compare different loan offers. The loan originator is only required to hand it out, but has the option of answering borrower questions about it. The short, simple, and self-explanatory nature of the form leads the Department to believe that the additional costs per form, if any, borne by an originator would approach zero.

Summary. To summarize, the discussion of the above factors identifies offsetting costs and suggests that there will be little if any additional annual costs associated with the new GFE. Practically all of the information required on the new GFE is readily available to originators, suggesting no additional costs. The fact that there are fewer numbers and less itemization of individual fees suggests reduced costs. The fact that the GFE figures are displayed on the HUD-1 will substantially simply the closing process. In addition, Section VII.D below lists further changes that HUD made to the form that are likely to reduce costs. On the other hand, there could be some small amount of additional costs associated with the optional trade-off table and documentation requirements. If there were additional costs of, for example, 10 minutes per GFE, the dollar costs would total $255 million per year (if the number of applications did not increase as a result of the result).[38] [39] But given the above discussion of offsetting effects and the improvements

[38] This calculation assumes a $150,000 fully-loaded annual salary; dividing by 2,080 hours yields $72 per hour, or $12 for ten minutes. Assuming 21,250,000 applications, produces a cost figure of $255 million. At 15 minutes, the cost estimate would rise to about $382.5 million. In the higher volume environment (26,350,000 applications), the overall cost figure would be $316.2 million if the per application cost was $12 for ten minutes.

[39] We have used a fully-loaded hourly opportunity cost of $72.12 for highly-skilled professional labor throughout the Economic Analysis. For many functions as well as locations this amount is probably an overestimate of the hourly opportunity cost. However, our goal in the Economic Analysis is to accurately measure the upper bound of the costs of the rule. An alternative method would be to generate an estimate of the average variable cost from industry-specific data. For example, in Tucson, Arizona, the average unit labor cost (salary, bonuses, time off, social-security, disability, healthcare, 401(k), and other benefits) is $30.73 per hour for loan officers ($23.97 for a Loan Officer/Counselor; $28.48 for a Consumer Loan Officer I; and $39.75 for a Consumer Loan Officer II). Additional costs to be considered are rent ($2812.50 per month for 1500 square feet) and computer equipment ($560 per month). Summing this gives us an hourly cost of $31.14. An additional ten minutes per application from handling the forms and ten minutes arranging tolerances leads to an additional twenty-seven minutes per closing and would increase

made to the form, there are likely to be no additional net costs with implementing the new GFE. Note, however, that there is the potential for recurring costs from changes to the HUD-1 . This issue is summarized in Section VIII.C.

Detailed Response to the NAR's Analysis of the 2008 IRFA

The National Association of Realtors provided an alternative estimate of compliance costs prepared by Ann Schnare (2008). The main thrust of their report was that HUD had grossly underestimated the compliance costs of the 2008 proposed rule. The following four sections summarize major comments relevant to estimates of the compliance costs of the new GFE.

Hedging Costs of the New GFE

Comment. The NAR's primary objection to HUD's estimates of the compliance costs of the proposed GFE was that HUD does not account for the hedging costs that an interest rate guarantee would require (Schnare 2008). Indeed, the majority of the NAR's cost estimate for the GFE consists of so-called "hedging" expenses. They claim that the rule would require issuers of GFEs to insure against interest rate movements to keep GFE offers open for the required 10 business days. According to the NAR report, the hedging costs could range from $136 to $272 per loan. Making this assumption dramatically increases the cost estimate for the GFE. The NAR's addition of hedging costs quadruples HUD's baseline estimate of the compliance cost of the proposed rule from $45 to $181.

Response. The NAR made an erroneous assumption about the proposed Good Faith Estimate (GFE) that lead them to overstate the compliance costs. A more accurate estimate of the hedging costs would be zero. Neither the proposed rule nor the final rule

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costs by $$14 per loan. The estimate of the recurring annual burden of the new GFE could reasonably be assumed to be $175 million, much less than the $405 million used throughout this analysis.

requires lenders to guarantee an interest rate quoted on a GFE for a period of ten days. Interest-dependent items on the GFE (interest rate, monthly payment, YSP/discount points, adjusted origination fees, and daily interest charges) can have a separate availability period that can be as short as the time until a new rate sheet is issued. Only the prices on non-interest-dependent items on the GFE (total origination fees, appraisal fees, title fees, etc.) must remain available for 10 days. These interest-rate-dependent items only become fixed, for purposes of comparison to the HUD-1 at closing, when the borrower locks the interest rate.

Indeed, the NAR study acknowledges that there is no such requirement. Ann Schnare writes: "HUD's revised GFE has multiple dates for the offer: one for the origination fee and third party settlement costs; one for the quoted interest rate; one for the settlement date; and one for the number of days that the loan must lock before closing (NAR, fn. 6, p. 10)." HUD let these dates differ because HUD is aware that the hedging costs of an interest guarantee for a period as long as ten days would be very costly.

The loan originator will probably choose a shorter guarantee period for the interest rate because of the hedging costs. Ann Schnare admits this to be a possibility: "the originator could choose a lock-in[40] period that is considerably shorter than the 10 business days required for other components of the GFE in order to minimize its hedging costs (NAR, p. 9)." Choosing the guarantee period of the interests rate is a profit maximizing decision made by the originator. The originator will balance the benefits of attracting more customers by extending the guarantee period with the hedging costs of doing so. The current practice of loan originators is to quote an interest rate and other

[40] HUD's understanding is that by "lock-in" period, the NAR meant "guarantee" period.

interest-rate-dependent rates with the caveat that the offer would change if market interest rates change. Since there is no reason to believe that hedging behavior will be affected by the rule, hedging costs should not be included as a compliance cost. Once this understanding of the proposed rule is introduced into the NAR's cost estimate of the proposed rule, the NAR's estimate falls from $181 to $45 (identical to HUD's estimate of the cost of the proposed rule) in their low-cost scenario; from $316 to $101 in their intermediate-cost scenario; and from $413 to $141 in their high-cost scenario.

Administrative Costs of More GFE Applications

Comment. A second major criticism by the National Association of Realtors of HUD's regulatory impact analysis of the 2008 proposed rule is that HUD underestimated the administrative costs of the proposed rule by not raising the number of loan applications per GFE. HUD's estimate of the ratio of applications to loans after the rule is implemented is equal to its estimate of the observed ratio of 1.7 in HMDA data. The NAR argues that the number of applications would rise because of increased shopping. Thus, the administrative costs of applications should rise.

Response. It is reasonable to expect that given the improvements to the GFE and the greater rewards from shopping, that the demand for applications would increase. Note, however, that maintaining a ratio of 1.7 loans per application is not inconsistent with more shopping for loan products. First, consumers may shop around and ask a variety of lenders for informal quotes to compare with their GFE. Every inquiry will not necessitate a new GFE. Second, the rule is likely to lead to lower rejection and withdrawal rates of applications because consumers will be more informed going into the loan. HUD expects applications from increased shopping behavior to replace some

mortgage applications that may have otherwise resulted in rejections. However, in response to this comment, HUD provides a sensitivity analysis of the effects on administrative costs of increasing applications per loan.

For reasons explained in the above paragraph, the number of applications per loan may remain at 1.7 applications per loan. If the additional administrative burden of an application imposed by the rule is ten minutes per application (as discussed in Section VII.C.1), then the additional burden of the rule translates to 17 minutes per loan (1.7 applications per loan X ten minutes). To derive the opportunity cost of the rule, we multiply 17 minutes by $1.20 per minute (equivalent to the $72 per hour fully-loaded opportunity cost of time, which comes from our $150,000 annual figure), to per loan cost of additional applications of $20.40 per loan. The aggregate impact on the loan origination industry of the administrative burden of completing applications is calculated using the per loan figure: the annual recurring compliance cost is $255 million (12.5 million loans annually X $20.40 per loan). The small business share of the total recurring compliance cost of this administrative burden is $134 million (52.2 percent of $255 million).

Suppose that the number of applications per loans increased by one from 1.7 to 2.7. This was one of the scenarios considered in the NAR's analysis. The NAR hypothesized that this is likely given that consumers may have a greater demand for a GFE once HUD's new GFE, which provides useful and transparent information, is introduced. Calculating the compliance costs due to the additional burden of completing GFEs is straightforward. The additional time spent per loan would be 27 minutes (2.7 application per loan X 10 minutes) and the opportunity cost of that time would be $32.40

per loan (27 minutes X $1.20 per minute). The total recurring compliance cost to the origination industry from applications would be $405 million (12.5 millions loan per year X $32.40 per loan), of which $213 million is borne by small business (52.2 percent of $405 million).

Multiple Preliminary Underwritings

Comment. Every application under the new rule requires preliminary underwriting. Since borrowers who shop may seek out multiple GFEs, there will be multiple underwritings. Commenters said this will add to the underwriting burden firms incur today. The National Association of Realtors calculated an additional cost of multiple underwriting at $30 per loan for an application per loan ratio of 2.7.

Response. Every application under the final rule that generates a GFE will require preliminary underwriting in order to come up with an early offer for the borrower. Originators can charge a fee for issuing a new GFE limited to the cost of a credit report. t is hoped that the charge for this, if any, would be small enough so that it is not a significant deterrent to effective shopping. But whether or not there is a charge, there are real resource costs associated with preliminary underwriting. The additional cost generated depends on the number of applicants and the number of GFEs they receive. Since every completed loan eventually gets underwritten in full, the additional cost of preliminary underwriting depends mainly on the number of additional times that preliminary underwriting occurs beyond the one associated with the full underwriting that would have occurred under the existing scheme.

It cannot be determined how many additional GFEs the average borrower would get under the new rule. Borrowers might continue the informal shopping method that

many use today – gathering information and making inquiries to lenders and brokers about their products and their rates, even before deciding to proceed with the request for a more formal quote using the GFE. In other words, they may formally apply only after deciding who offers the best terms. The simple format and clarity of the new GFE form will enhance this informal information gathering process; in fact, the increased efficiency of informal shopping (calling around, checking web sites, etc.) could be an important benefit of the new GFE. Since shoppers as well as originators will be familiar with the GFE, these forms will likely serve as a guide for practically any conversation between a shopper and an originator, or for any initial request by a shopper for preliminary information about rates, points, and fees. For these borrowers, the new GFE simply pins down the numbers. Others, on the other hand, may obtain multiple GFEs and use them to shop.

Under the final rule, preliminary underwriting should decrease the number of applications that go to full underwriting (e.g., an applicant may be denied during the preliminary without having been charged for an appraisal); that is, some of the 8.75 million that are not originated may be disapproved at the preliminary stage rather than going through full underwriting (as they might today). This savings in appraisal, verification, and other incremental underwriting costs that are avoided would tend to offset the increase in cost resulting from the extra preliminary underwriting noted in the above paragraph. However, it is difficult to estimate these effects.

An implication of a higher ratio of applications per loan is that the total underwriting costs would increase. Others, on the other hand, may obtain multiple GFEs and use them to shop. The National Association of Realtors estimates that the cost of a

preliminary underwriting is $30 ($25 credit report and $5 labor cost). There are currently 1.7 times as many applications as loans originated. Thus, the additional cost per loan for the scenario of 2.7 applications per loan is $30 ((2.7-1.7) X $30) and for 3.4 applications per loan, the additional cost is $52 ((3.4-1.7) X $30). HUD uses different parameters to estimate the cost of increased applications. Instead of a preliminary credit report cost of $25, HUD would use $5. This lower number is not inconsistent with HUD's estimated cost of $25 for a full credit report. A preliminary credit report involves only the FICO score from one credit bureau and so will be much cheaper. Our assumption of an inexpensive preliminary credit report is consistent with what representatives of credit bureaus, in discussions of the effects of the proposed rule, told HUD is likely to happen. Instead of labor costs of $5 (ten minutes at $31.14 an hour); HUD uses $6 (five minutes at $72 an hour). HUD's estimated total cost of a preliminary underwriting would be $11, reducing the additional costs from $30 to $11 at 2.7 applications per loan.

The aggregate impact on the loan origination industry of multiple preliminary underwriting is calculated using the per loan figure: the annual recurring compliance cost is $138 million (12.5 million loans annually X $11 per loan) at 2.7 loans per application. The small business share of the total recurring compliance cost from additional underwriting is $72 million (52.2 percent of $138 million). If the ratio of applications per loan does not change (remains at 1.7), then there will be no additional compliance cost from multiple preliminary underwriting.

Finally, it should be emphasized that, under the final rule, preliminary underwriting should decrease the number of applications that go to full underwriting (e.g., an applicant may be denied during the preliminary without having been charged for

an appraisal). Some of the assumed 8.75 million applications[41] that are not originated may be disapproved at the preliminary stage rather than going through full underwriting (as they might today). We expect an increase in the ratio of accepted applications per loan. This savings in appraisal, verification, and other incremental underwriting costs that are avoided would tend to offset the increase in cost resulting from the extra preliminary underwriting noted above.

Estimate of the Opportunity Cost of Time

Comment. The National Association of Realtors states (see NAR 2008, fn. 10, p. 11) that HUD used one estimate of the value of an employee's time ($31.14 per hour) to calculate the burden of the proposed rule but a higher estimate ($72 per hour) of the opportunity cost of time to calculate the benefits of the time savings of the proposed rule.

Response. HUD uses the estimate of $72 per hour as the opportunity cost of time consistently throughout the regulatory impact analysis to calculate the value of the costs and the benefits of the rule to industry. It is true that HUD includes a discussion of alternative estimates of labor costs in a footnote of Chapter 6 (see below)37 on page 6-6 of the Regulatory Flexibility Analysis. There, HUD explains that our estimate of $72 per hour may be far above other estimates of labor costs. HUD provides an example of an estimate based on industry data from Tucson, Arizona, where the hourly-wage weighted by industry is $31.14. However, this figure was only presented for illustrative purposes and was not used in the body of the analysis. Note also that HUD uses a lower value of $44 per hour as the opportunity cost of time to consumers (see HUD, 3-120)

[41] There are currently 1.7 times as many applications as loans originated; therefore, if originations are 12.5 million, full underwriting is started (and probably completed) for about 21.25 million applications, including 8.75 million (21.25 million minus 12.5 million originations) that are not originated.

The NAR uses the $31.14 hourly wage as a measure of the opportunity cost of an employee's time in their cost estimates of additional underwriting. However, they do not apply this figure consistently throughout their analysis and do not explain why. Because $31 is only 43% of $72, a uniform application of the NAR labor cost estimate would lower the burden of the rule significantly. For example, the recurring costs of the GFE would fall from $32 per loan to $14 in the case of 1.7 applications per loan. Although HUD will consider the NAR's preference for a lower estimate of labor costs, HUD believes that its fully-loaded and upper-bound estimate of $72 is more appropriate for a regulatory impact analysis.

Tolerances on Third-Party Fees

Under the March 2008 proposed rule, loan originators would have been prohibited from exceeding at settlement the amount listed as "our service charge" on the on the GFE, absent changed circumstances ("zero tolerance"). The proposed rule also would have prohibited the amount listed as the charge or credit to the borrower for the interest rate chosen, if the interest rate was locked, absent unforeseeable circumstances, from being exceeded at settlement. In addition, the proposed rule would have prohibited Item A on the GFE, "Your Adjusted Origination Charges" from increasing at settlement once the interest rate was locked. The proposed rule also would have prohibited government and recording fees from increasing at settlement, absent changed circumstances.

Under the March 2008 proposed rule, the sum of all the other services subject to a tolerance (originator-required services where the originator selects the third party provider, originator-required services where the borrower selects from a list of third party providers identified by the originator, and optional owner's title insurance, if the

borrower uses a provider identified by the originator) would have been prohibited from increasing at settlement by more than 10 percent of the sum for services presented on the GFE, absent changed circumstances. Thus, a specific charge would have been able to increase by more than 10 percent, so long as the sum of all the services subject to the 10 percent tolerance did not increase by more than 10 percent.

The rational for the zero tolerance was that a loan originator should know the price of a service if it required the use of its chosen provider. In the case of making referrals, the loan originator could be expected to have some knowledge of the market. In fact, it should have some knowledge if it is to meet even the weakest concept of "good faith." The 10 percent tolerance seemed like a reasonable limit for price dispersion for services obtained in a market that could be competitive if the buyers had good information. It is also simple for borrowers quickly to compute 10 percent of the total fee and determine if final charges are within the tolerance. In order to protect themselves from charges in excess of the limits set by the tolerances, originators would have to gather price information in the market and possibly set up agreements with some third-party providers to perform settlement services at prearranged prices. Those originators who would have gathered more information than they do today or made more pricing arrangements than they do today would have incurred an increase in regulatory burden resulting from the new rule.

Comment. Loan originators wrote that they should not be required to pay the bills for third–party fees in excess of the tolerances since they do not control those fees. They argued that their expertise is as originators, not as appraisers or title companies. They claimed that they do not know who will perform all these services at application, so the

price is indeterminate. In addition, there are occasions when services beyond the normal minimum will be required, but that cannot be known at application. For example, additional appraisal work may be required or some work may have to be done to clear up a title problem. So prices and even some services that end up as being required are unknown at application.

Trade groups representing settlement service providers, especially realtors and title companies, focused on the potential anticompetitive effects of the tolerance provisions. These groups suggested that large lenders would seek to manage the risks associated with tolerances by contracting with large third party settlement service providers, and thereby placing small settlement service providers at a competitive disadvantage.

In addition to their general objections to the tolerance provisions, lenders and trade groups representing lenders and other settlement service providers strongly supported removing government recording and transfer charges from the tolerances. They stated that these charges are outside of the control of the loan originator and cannot be known with any certainty at the time the GFE is provided.

If the loan originator solves its problem by using only those third-parties that agree to fixed prices, that shifts the burden to the third-party. Small third-party providers made the same argument that small originators made. They then will be disadvantaged relative to large third-party providers by having to bear the risk of the unpredictable cost that cannot be averaged out over a large number of transactions.

Response. Based on the comments received in response to the proposed rule, HUD has revised a number of provisions dealing with the tolerances, and in particular

has clarified the situations where the loan originator would no longer be bound by the tolerances. However, HUD has determined that only limited changes are necessary in the tolerances themselves. Through all of these provisions, the final rule seeks to balance the borrower's interest in receiving an accurate GFE early in the application process to enable the borrower to shop around, with the lender's interest in maintaining flexibility to address the many issues that can arise in a complex process such as loan origination.

Many commenters recommended changes to the size of the tolerances for different categories of settlement costs, especially the zero tolerance for loan originator charges. With one exception (government recording and transfer charges), the final rule does not change the amounts of the tolerances permitted for the different categories of settlement costs. As noted in the rule, HUD considered the best available data on the variation in the costs of settlement services, in particular title services, in determining that a 10 percent tolerance is reasonable. No commenters submitted or identified any alternative data sources that would support expanding the tolerances beyond 10 percent.

With respect to the zero tolerance for a loan originator's own charges, HUD recognizes the comments characterizing the tolerance as a settlement cost guarantee. However, the final rule provides substantial flexibility to loan originators in providing a revised GFE when circumstances, unforeseeable or otherwise, necessitate changes. Section 19(a) provides explicit authority for the Secretary to make such interpretations as may be necessary to achieve the purposes of RESPA. Providing a clear, objective standard for what constitutes "good faith" under section 5 of RESPA is necessary to provide more effective advance disclosure to home buyers and sellers of settlement costs,

and as such, falls directly within the Secretary's interpretive authority under section 19(a).

The one exception to the amounts of the tolerances remaining the same as in the proposed rule is the tolerance for the government recording and transfer charges. HUD has adjusted how these charges are treated under the tolerances, based on the numerous comments received on this issue. The final rule splits the government recording and transfer charges into two categories: government recording charges, and transfer taxes. Recording charges will be subject to a 10 percent tolerance instead.

The opportunity to cure potential violations of the tolerances is an important tool for loan originators to manage compliance with the tolerance requirements. Many lenders and groups representing lenders and other settlement service providers objected to the imposition of tolerances because of the difficulty of providing accurate estimates to prospective borrowers early in the application process. The opportunity to cure will permit loan originators to give an estimate of expected settlement charges in good faith, without subjecting them to harsh penalties if the estimate turns out to be lower than the actual charges at settlement.

HUD understands that tolerances will impose some burden on originators. Since the protection of tolerances kicks in only if the originator requires the use of a particular provider or if the borrower comes to the originator and asks where the services may be purchased within the tolerances, the originator must have reliable third-party settlement service provider pricing information. Some originators might simply check out the market prices for third-party services from time to time, formulate estimates such that several of the prices charged by the third parties fall within the tolerance, and trust that

nobody to whom they refer the borrower charges a price in excess of the tolerance[42]. Other originators might want more protection and have contracts or business arrangements in place that have set prices for services that are not in excess of the tolerances.

Either case requires the originator to do more than today, although even today originators fill out GFEs with estimates for third-party settlement services. In the first case, the liability in the event a tolerance is exceeded would lead to at least a little more work gathering information prior to filling out the GFE. In the second case, more work would be involved in formalizing an agreement to commit the third-party to a fixed price. But as noted above, originators today have to have a working knowledge of third-party settlement service prices to fill out a GFE. Therefore, it is only the increase in burden that would need to be accounted for here.

It is difficult to estimate these incremental costs. But to provide an order of magnitude, it is estimated that it takes an average of 10 additional minutes per loan for the originator to arrange the pricing that protects the originator from the costs of the tolerances being exceeded.[43] For a brokerage firm originating 250 loans per year, 10 minutes per loan would come to 42 hours or about one week's worth of one employee's time per year. Thus, this seems to be a reasonable starting point for estimation. For the estimated 12,500,000 loans, that comes to 125,000,000 minutes or 2,083,333 hours. At $72 per hour, which translates to $12 per loan, this comes to a total of $150 million for all firms and $78 million for small firms. If it takes 20 extra minutes per loan instead of 10,

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[42] Other originators may rely on vendor management companies (or vendor management departments within their own company) for pricing information about third-party services.
[43] These 10 minutes would be beyond what the originator spends today to seek out good choices for his borrowers.

these costs come to $300 million and $156 million respectively and would be two weeks of one employee's time per year for a brokerage firm making 250 loans per year. Table 6-12 details the distribution of these costs among the retail mortgage originating industries for the per loan burden of ten minutes. With a larger number of loans (15,500,000), total costs are $186 million for all firms (at 10 minutes per loan) and $97 million for small firms.

Table 6-12 Incremental Costs of Third-party Pricing Arrangements for the New GFE

Industry	Total Third-party Pricing Arrangement Cost	Small Business Cost
Mortgage Brokers	$90,000,000	$63,000,000
Commercial Banks	$24,637,800	$4,678,718
Thrifts	$11,697,000	$1,441,070
Mortgage Banks	$18,618,000	$7,737,641
Credit Unions	$5,047,200	$1,470,754
TOTAL	$150,000,000	$78,328,183

One wholesale lender, ABN-AMRO, offers a One-fee program to brokers. In it, the borrower gets a fixed price for many services, including many third-party services. Under the new GFE, arrangements like this would solve the broker's tolerance compliance requirements with the wholesaler making the arrangements for many of the third-party services and negotiating the prices for them. So it may be that (mostly large) wholesalers offer (mostly small) brokers a lower cost alternative to complying with the tolerance requirements of the new rule. If so, then the small business burden above would be an overestimate. Vendor management companies are increasingly appearing in

the market, not only providing third-party pricing information, but also offering monitoring and quality control services for originators.

Changes in the Final Rule to Reduce the Regulatory Burden of the GFE[44]

The final rule contains several changes from the 2008 proposed rule that are designed to reduce regulatory burden of the new GFE. Several items that commenters were concerned about have been changed from the 2008 proposed to the final GFE:

- Length of form. Many industry groups complained that the four-page proposed GFE was too long. HUD reduced the form in the final rule to three pages by consolidating the third and fourth pages but still retaining the essential trade-off table and shopping chart.

- Concept of "GFE application" Commenters objected to the bifurcated application process (a preliminary "GFE application" followed by the final "mortgage application"), which was designed to promote shopping. There was a fear of commitment by lenders to loan terms based on a preliminary underwriting, as well as fear that that the preliminary underwriting would be based on information that was too limited (borrower's name, social security number, gross monthly income, property address; an estimate of the value of the property; and the amount of the mortgage loan sought). In response, HUD has adopted a single application process for the final rule. Under this approach, at the time of application, the loan originator will decide what application information it needs to collect from a borrower, and which of that collected application information it will use, in order to issue a meaningful

[44] See Chapter 3 for or a treatment of changes listed in this section.

GFE. HUD strongly urges loan originators to develop consistent policies or procedures concerning what information it will require to minimize delays in issuing GFEs.

- Volume-based discounts. Small businesses, especially closing attorneys and escrow companies stated that lenders seeking volume discounts would place them at a competitive disadvantage to larger entities and force them out of business. HUD responded by not addressing volume discounts in its final rule.

- Difficulty of meeting tolerances. Many lenders and groups representing lenders and other settlement service providers objected to the imposition of tolerances because of the difficulty of providing accurate estimates to prospective borrowers early in the application process. The final rule provides loan originators with an opportunity to cure any potential violation of the tolerance by reimbursing the borrower any amount by which the tolerances were exceeded. The opportunity to cure will permit loan originators to give an estimate of expected settlement charges in good faith, without subjecting them to harsh penalties if the estimate turns out to be lower than the actual charges at settlement.

Costs Associated with Changes to the HUD-1

This section discusses costs on closing agents associated with the new HUD-1. Section VIII.A explains the data and VIII.B the analysis of costs.

Data on Settlement Service Providers

Section VII.A reproduced background data on the retail mortgage origination industries. Since the GFE affects settlement service providers as well as retail mortgage

originators, this section recapitulates data from Chapter 5 on the settlement services industries. Readers are referred to Section IV of Chapter 5 for a more detailed treatment of the data.

Table 6-13 provides the total number of firms, the number of small employer firms, the number of nonemployer firms, and the percent of small firms (employer and nonemployer) in industries that provide settlement services (see Chapter 5 for details on the classification of small employer firms in these industries). These constitute all of the firms in these industries in 2004, according to the Census Bureau. As discussed below, for Offices of Lawyers, Other Activities Related to Real Estate (Escrow), Surveying & Mapping Services, Extermination & Pest Control Services, and Credit Bureaus, the figures in Table 6-13 almost certainly overstate the number of firms actually participating in residential real estate settlements.[45]

[45] As shown by the fourth column, practically all firms qualify as small businesses. This is partially due to the large number of non-employer firms (which automatically qualify as a small business) included in the Bureau of Census data. See Chapter 5 for further discussion of this issue and for small business percentages for employer firms only. Also note that while the number of firms is drawn from year 2004 data, the small business percentages are based on 2002 data from the Bureau of Census; while they are estimates, they are probably highly accurate ones. Also see Chapter 5 for the source of the small business percentages and for alternative, year-2002-based small business percentages based on firms with less than 100 employees.

Table 6-13. Firms in Industries Providing Settlement Services

Industry	Total Firms	Small Employer Firms	Nonemployer Firms	Percent Small Firms
Direct Title Insurance Carriers	2,094	1,865	135	95.5%
Title Abstract and Settlement Offices	14,211	7,889	6,203	99.2%
Offices of Lawyers	401,553	165,127	234,849	99.6%
Other Activities Related to Real Estate (Escrow)	463,545	15,119	448,409	99.996%
Offices of Real Estate Appraisers	65,491	15,656	49,802	99.9%
Surveying & Mapping Services	18,224	8,990	9,196	99.8%
Extermination & Pest Control Services	18,000	10,018	7,935	99.7%
Credit Bureaus	1,285	710	545	97.7%
TOTAL	984,403	225,374	757,074	99.8%

SOURCE: Census Bureau

Table 6-14 provides the total number of employees in employer firms, and the number and percent of employees in small employer firms for each of the settlement services industries.[46] The Census Bureau does not count owners of employer and non-employer firms as employees. The number of "workers" in these industries is understated by the number of employees as defined by the Census Bureau because in a

[46] The "Total Employees" data in Table 6-10 are for the year 2004. The "Employees in Small Employer Firms" data are obtained by multiplying the total employee data for 2004 by the percentage of employees in SBA-defined small firms obtained from 2002 Bureau of Census data; thus, the small employee data are estimates but probably highly accurate ones. See Chapter 5 for discussion of the 2002 small business percentages.

nonemployer firm the owner is a production worker as is likely also true for the owner of a small employer firm. Using the Census Bureau's count of employees for computing the compliance burden of a rule may tend to understate the burden.[47] Thus in computing the number of workers in these industries, one worker is added for each small employer firm and each nonemployer firm to the total number of employees (see Table 6-16 below for these results).

[47] For example, if worker training were required by the rule, and burden estimates were based on Census Bureau employee statistics, the compliance burden for nonemployer firms would be estimated at zero, while clearly at least one "worker," the owner, would require the training.

Table 6-14. Employees In Industries Providing Settlement Services

Industry	Total Employees in Employer Firms	Employees in Small Employer Firms	Percent Employed by Small Firms
Direct Title Insurance Carriers	75,702	7,144	9.4%
Title Abstract and Settlement Offices	79,819	47,913	60.0%
Offices of Lawyers	1,122,723	657,749	58.6%
Other Activities Related to Real Estate (Escrow)	67,274	40,074	59.6%
Offices of Real Estate Appraisers	45,021	37,300	82.8%
Surveying & Mapping Services	61,623	53,610	87.0%
Extermination & Pest Control Services	95,437	55,565	58.2%
Credit Bureaus	25,555	5,135	20.1%
TOTAL	1,573,154	904,490	57.5%

SOURCE: Census Bureau (note: non-employer firms not included)

Table 6-15 provides information on the volume of settlements for various industries that participate in the settlement process and the number and percent handled by small firms within each industry.[48] Note that while the distribution among Direct Title

[48] The small business percentages in Table 6-12 are the shares of revenue accounted for by small business, as reported and explained in Chapter 5 – in other words, the small business share of revenues is being used here as a proxy for the small business share of settlements (or mortgage loans). There are two other points that should be made about these data. (1) Figures for Offices of Lawyers and Other Activities Related to Real Estate (Escrow) are combined into the new "Lawyers and Escrow" category. This is because there is

Insurance Carriers, Title Abstract and Settlement Offices, Offices of Lawyers, Lawyers and Escrow, Offices of Real Estate Appraisers, and Credit Bureaus is based on all settlements, the numbers and percentages for the other industries (Surveying & Mapping Services and Extermination & Pest Control Services) represent the proportion of settlements in which they are involved.[49] The allocation is based upon estimated dollar revenues from settlements for these industries.[50] Totals are estimated based on the number of mortgage originations, 12,500,000 that would occur in a "normal" year of mortgage originations (i.e., not in a year with a refinancing boom).

Table 6-15. Volume of Settlement Service Activity

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insufficient information to allocate volumes of settlements between these two industries (see Section IV.B.5 of Chapter 5 for further explanation). As explained in Chapter 5, the small business revenue share for the combined "Lawyers and Escrow" category is raised to 90% (versus 47.8% for all lawyers and 86.9% for escrow firms based on 2002 Census Bureau revenue data) under the assumption that lawyer and escrow firms engaged in real estate activity are likely to be the smaller firms operating in these industries. Note that in Table 6-13 below, the 90% figure is also used for the share of employees in small firms in this combined industry. (2) As explained in Section IV.B.4 of Chapter 5, there are probably no small businesses in the Direct Title Insurance Carriers (DTIC) industry, which includes the large title insurance firms. The 4.8% figure in Table 6-12 (as well as the 9.4% figure in Table 6-10) is reported to remain consistent with the Bureau of Census data – including it or excluding it does not affect the results in any significant way.

[49] See Step (9) in VII.E.1 of Chapter 3 for the calculation of the proportion of settlements for Surveying & Mapping Services and Extermination & Pest Control Services. Because of their relatively small shares of the overall mortgage business, different shares for these industries would not materially affect the overall small business shares of revenue. While it is recognized that the other industries may not be involved in every mortgage origination and settlement transactions (e.g., an appraisal may not be required for some mortgage originations), they are certainly involved in most such transactions and, therefore, it is assumed here that they are involved in all transactions.

[50] As explained in Chapter 5, there is also some uncertainty about the distribution of mortgage-related business and revenues among the various title-related industries. Table 6-12 assumes the following distribution: Direct Title Insurance Carriers (43.0%), Title Abstract and Settlement Offices (38.0%), and Lawyer and Escrow (19.0%). Section IV.B.5 of Chapter 5 considers other distributions and suggests the following ranges for the specific industry shares: Direct Title Insurance Carriers (35%-50%), Title Abstract and Settlement Offices (29%-43%), and Lawyer and Escrow (17%-29%). Given limited available information, it is difficult to determine a precise estimate, which is why Chapter 5 includes several sensitivity analyses. But obviously, reducing the relative weight of the DTIC or increasing the relative weight of the lawyer-escrow industry would increase the small business share of settlements. Readers are referred to Section IV of Chapter 5 for a more complete analysis of the relative importance of each title-related industry, particularly as it affects the overall small business percentage for title- and settlement-related work.

Industry	All Settlements	Percent of Settlements	Settlements by Small Firms	Percent Industry Settlements by Small Firms
Direct Title Insurance Carriers	5,375,000	43.00%	258,000	4.80%
Title Abstract and Settlement Offices	4,749,953	38.00%	2,365,476	49.80%
Lawyers and Escrow	2,375,048	19.00%	2,137,543	90.00%
TOTAL SETTLEMENTS	12,500,000	100.00%	4,761,019	38.09%
Offices of Real Estate Appraisers	12,500,000	100.00%	10,387,500	83.10%
Surveying & Mapping Services	3,600,000	28.80%	2,926,800	81.30%
Extermination & Pest Control Services	5,500,000	44.00%	2,964,500	53.90%
Credit Bureaus	12,500,000	100.00%	1,312,500	10.50%

A larger volume of mortgage activity can also be examined, for example, to reflect a "refinance environment".[51] In this case, the volume of settlement activity would be distributed as follows: 6,665,000 for Direct Title Insurance Carriers, 5,889,941 for Title Abstract and Settlement Offices, 2,945,059 for Lawyers and Escrow, 4,464,000 for Surveying & Mapping Services, 6,820,000 for Extermination & Pest Control Services, and 15,500,000 for both Offices of Real Estate Appraisers and Credit Bureaus.[52]

[51] In the projection given in the text, home purchase loans were assumed to stay the same (7.5 million, or 60% of the 12.5 million in mortgages), while refinances increased from 5 million (or 40% of the 12.5 million mortgages) to 8 million of the 15.5 million total (home purchases remain at 7.5 million).
[52] The settlement volume for small businesses during a high volume year can be obtained using the small business percentages from Table 6-12, giving: 319,920 for Direct Title Insurance Carriers, 2,933,191 for

The employee figures reported in Table 6-14 misstate the number of workers actually participating in residential real estate settlements. This section offers some estimates of that figure, although it is recognized that they are subject to some uncertainty given the limited information that is available. Table 6-16 provides one estimate of the total number of workers and the number and percent of workers in small firms engaged in performing settlements by industry. For Title Abstract and Settlement Offices and the combined Lawyers and Escrow industry, it is based on the volumes of settlement activity depicted in Table 6-15 and the productivity level of Title Abstract and Settlement Offices (i.e., settlements per worker).

The figure for total workers in Title Abstract and Settlement Offices is the sum of: all employees (79,819), small firms (7,889), and nonemployer firms (6,203), or 93,911. (Small firms and nonemployer firms are added to count the owners of those firms as production workers as discussed in the description of Table 6-14 above). The corresponding figure for workers in small firms is the sum of: employees of small firms (47,913), small firms (7,889), and nonemployer firms (6,203), or 62,005 workers (representing 66% of all workers in Title Abstract and Settlement Offices). These figures are reported in Table 6-16 below. In this industry, there are 50.6 settlements per worker (obtained by dividing the 4,749,953 settlements from Table 6-15 by the 93,911 workers).[53]

Title Abstract and Settlement Offices, 2,650,553 for Lawyers and Escrow, 3,629,232 for Surveying & Mapping Services, 3,675,980 for Extermination & Pest Control Services, 12,880,500 for Offices of Real Estate Appraisers, and 1,627,500 for Credit Bureaus.

[53] There are two caveats with this estimate. First, the estimate depends on the number of settlements in the Title Abstract and Settlement industry, which, as discussed in an earlier footnote, could differ from the number reported in Table 6-12 (see Section IV.B.5 of Chapter 5 as well as the earlier footnote for possible ranges of estimates). Second, not all workers in the Title Abstract and Settlement industry are engaged in single-family real estate transactions, which means that the number of workers is overstated and therefore

In the combined Lawyers and Escrow industry group, worker productivity is assumed to be half of that in Title Abstract and Settlement Offices on the grounds that these workers may not do settlements full time and because of the general lack of information on the degree of settlement activity in these broadly defined industries. Thus, the number of workers in this category (93,914) is computed by dividing the number of settlements handled by the industry from Table 6-15 divided by one-half the settlements per worker in the Title Abstract and Settlement Offices industry.

For Direct Title Insurance Carriers, many workers are not engaged in actual settlements, but rather in the title insurance function itself. Direct Title Insurance Carriers provide title insurance through agents as well as both direct sales of title insurance and associated settlement services to consumers through branch offices. They also, of course, perform the title insurance function itself. HUD examined the annual reports of the large direct title insurance carrier companies to attempt to estimate the proportion of employees of these companies engaged in providing settlement services. It is estimated that approximately 70 percent of workers in this industry, or 54,391 workers, are engaged in providing settlement services. (See Table 6-16).[54]

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the number of settlements per worker is understated. (Unfortunately, there is no information on the proportion of Title and Abstract workers engaged in single-family mortgage activity, although it is likely that most are.) If the number of settlements per worker is too low, the projection will overstate the number of workers needed.

[54] In 2004, the DTIC industry employed 77,702 workers (based on the definition of worker used in the text). HUD estimates that approximately 70 percent, or 54,391, are engaged in providing settlement services. HUD computed an estimate of the proportion of salaries that large title insurance companies paid to workers engaged in settlement services as follows: (1) the amount of revenue required to carry out the insurance function for policies written by agents was computed as the difference between agent-generated revenue and agent commissions (or agent retention expenses); (2) two percentages were then calculated, (a) the percentage of agent-generated revenue required for the insurance function in agent-written policies as (1) divided by total agent-generated revenue, (b) the percent of all insurance revenue required for the insurance function for agent-written policies as (1) divided by total insurance revenue; (3) the salaries for employees providing the insurance function for agent-written policies was computed by multiplying (2)(b) by total salary expenses; (4) the total salaries for employees engaged in direct sales of insurance (including

Table 6-16. Workers Engaged Performing Settlements

Industry	Total Workers	Workers in Small Firms	Percent of Workers in Small Firms
Direct Title Insurance Carriers	54,391	6,401	11.77%
Title Abstract and Settlement Offices	93,911	62,005	66.03%
Lawyers and Escrow	93,914	84,523	90.00%
TOTAL	242,217	152,929	63.14%

The estimated numbers of title and settlement workers would be larger under market conditions producing a larger volume of mortgage activity. The estimated distribution of settlements when overall mortgage volume is 115,500,000 was given earlier. To adjust the worker estimates in Table 6-16 to reflect the higher mortgage volume requires information about the increase in productivity (i.e., loans per worker) during the higher volume (or heavy refinance) environment. It is not correct to simply adjust the number of workers up by the percentage increase in mortgage loans because the number of loans per worker increases during refinance booms. The earlier analysis of brokers and lenders provided estimates of additional workers in a higher volume market. That analysis was based heavily on trend data through 2002 for the number of workers in

other settlement services) and providing the insurance function for direct-sales policies was computed by subtracting (3) from total salary expenses; (5) the salaries of employees providing the insurance function for direct-sales policies was computed by multiplying (2)(a) by (4); (6) the salaries of employees selling title insurance directly (and providing other settlement services) was computed by subtracting (5) from (4); finally (7) the percent of salaries paid to employees selling title insurance directly (and providing other settlement services) was computed by dividing (6) by total salary expenses. This analysis was carried out using 2005 data from the annual reports of four title insurance companies (First America, Land America, Fidelity National, and Stewart). The percentage computed in (7) ranged from 67.7 percent to 72.8 percent. Based on these results, HUD assumes that 70 percent of DTIC workers are engaged in providing direct title insurance sales and other settlement services.

the broker industry, as reported by David Olson and his firm, Wholesale Access. The number of loans per broker increased between low and high volume years. Similar trend data do not exist showing the number of title and settlement workers during recent refinance booms. Thus, any adjustment would be somewhat speculative. But it is also important to emphasize that workers hired during high-volume years, for example, are more likely to be temporary or part-time workers. Temporary workers will likely rely on permanent workers for training or information about new rules and regulations. Thus, the numbers in Table 6-16 providing estimates of workers in the title and settlement industry serve as a reasonable basis for analyzing the effects of the new regulation among the various settlement and title industries, recognizing that the numbers could vary somewhat depending on the volume of mortgages considered in the analysis.

Estimates of the number of single-family-mortgage-related workers in Surveying & Mapping Services, Extermination & Pest Control Services, and Credit Bureaus are not included because there are insufficient data upon which to base an estimate. Mortgage-related work accounts for a relatively small portion of the overall activity of these industries, and information is not available to separate single-family-mortgage-related business from other activity. In addition, data on workers for these industries are not needed for the analysis of cost savings below. While this information is also not needed below for the appraisal industry, it is possible to produce reasonable estimates of workers for this industry because single-family-mortgage-related work likely accounts for most of the activity in this industry. Using the methodology described above (adding employees of employer firms, non-employer firms, and owners of small firms to arrive at the number of workers), the appraisal industry in the projection year would include 110,479 workers,

and 102,758 of these work in small firms.[55] While some of these appraisers focus on multifamily and commercial properties and/or conduct appraisals for local governments (e.g., estimating the value of properties for tax purposes), most are likely involved in single-family mortgage-related activities.[56]

One-Time Costs of the New HUD-1

Introduction

The new HUD-1 is simpler than the existing HUD-1. Nevertheless, there will be change in the form, including the introduction of the comparison page, and the settlement industry will need to learn how the new form works. The primary focus will be on how to put the numbers in the right place. The major changes in the HUD-1 itself are to make it more comparable to the GFE. Accordingly, to facilitate comparison between the HUD-1 and the GFE, each designated line in Section L on the final HUD-1 includes a reference to the relevant line from the GFE. Borrowers will be able to easily compare the designated line on the HUD-1 with the appropriate category on the GFE. Terminology on the HUD-1 has been modified as necessary to conform to the terminology of the GFE. For example, since Block 2 on the GFE is designated as "your credit or charge for the specific interest rate chosen", Line 802 on the HUD-1 is also designated "your credit or charge for the specific interest rate chosen."

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[55] The total number of workers is derived as follows: 45,021 employees in employer firms (from Table 6-14) plus 49,802 non-employer firms (from Table 6-13) plus 15,656 owners of small firms (from Table 6-13), which yields 110,479 workers. The number of workers in small businesses is derived as follows: 37,300 employees in small employer firms (from Table 6-14) plus 49,802 non-employer firms (from Table 6-13) plus 15,656 owners of small firms (from Table 6-13), which yields 102,758 workers in small businesses.

[56] One would think that practically all of the owners of the 49,802 non-employed firms appraised single-family properties, as well as most of the 37,300 employees in small employer firms. One could argue that the number of workers for the entire industry in 2004 is a upper bound since mortgage activity in that year was higher than in the projection year. Additionally, automated valuation models (AVMs) may have reduced the demand for appraisers; particularly on refinance loans (see Section V.A of Chapter 5 for a discussion of AVMs).

The comparison page of the HUD-1, which is an additional page, will represent a more significant change for the industry than the slight revisions of the current pages. Although some training may be required, it is not likely to be substantial since settlement agents are already very familiar with what information to provide at a closing. The comparison page displays any differences between the settlement charges on the GFE and the HUD-1 on the top half. On the bottom half of the comparison page, there is a summary of loan, in a manner similar to the GFE. The burden of the comparison page of the HUD-1 is most likely to be felt as a one-time adjustment cost imposed on software developers. In response to the March 2008 proposed rule, many lenders expressed the concern that the way the new HUD-1 forms are to be completed would require numerous changes with significant operational and technology impacts. These costs can be categorized similarly as for the new GFE: software costs (including training), legal consultation costs, and training costs. The total one-time compliance cost to the industry is $188 million, of which $139 million is borne by small business.

Settlement Software Costs

Developers of settlement software and settlement agents will be subject to software costs. They will face the following two changes: a reorganization of the HUD-1 form and the requirement of the HUD-1 comparison page explaining the crosswalk between the GFE and the final HUD-1. The changes to the HUD-1 form would not require much work from programmers. The only programming to be done is changing the manner in which information is displayed on the HUD-1 form. First, there will be fewer fees. Second, references to the corresponding figures in the GFE would need to be inserted by the software developers.

Including the comparison page would require more effort because it is completely new. The programming itself would not be challenging since the new page only contrasts data from the HUD-1 and the GFE, shows whether the tolerances are met, and displays data concerning loan terms. The more complex calculations concerning the loan terms are not required to be done by the settlement agent but by the lender. Loan originators must transmit settlement cost and loan term data to the settlement agents for page 3 (the comparison page) of the HUD-1 form. As discussed previously, lenders will provide most, if not all, of the data for the comparison page of the HUD-1. Settlement agents will need new software for the simple reason that the form will change. There will also be a strong demand by settlement agents for new software that checks the tolerance calculations given the importance of the comparison page as a means to double check the final figures.

We will assume that the costs of software updates and software training to the settlement industry are the same as for the new GFE. Given the number of workers and the distribution by firm size, the total cost of new software and training is $62 million, of which $46 million is borne by small business. The cost of the changes to software is $14 million (of which $11 million is borne by small business) and the opportunity cost of the time spent learning the new software is $48 million (of which $34 million is borne by small business).

To arrive at a total one-time cost for the HUD-1, we add the additional cost of $18 million of new loan origination software as a result of the HUD-1 to the $62 million for the settlement industry's new software, which yields a total one-time software cost of $80 million to the entire industry. Adding the $13 million of HUD-1 related software costs

from small loan originators to the $46 million imposed on small settlement firms yields a total of small business one-time compliance costs of $59 million.

Legal Consultation Costs

Legal consultation will be less involved for the HUD-1 form than for the new GFE. However, settlement firms may require additional legal consultation to inform on a diverse set of issues, such as average cost-pricing, to be on the safe side. We make the same assumptions as for the GFE: all firms purchase a minimum of two hours of legal consultation at a cost of $200 an hour and that additional legal service are demanded on the basis of the volume of business. We estimate that the total legal costs to the settlement industry will be $37 million of which $18 million is borne by small business. The cost of legal fees is lower for the HUD-1 form than for the GFE because there are less firms involved in settlement than in mortgage origination.

Training Costs

Workers who perform settlements will need to learn how to fill out the new HUD-1 form and in some cases, calculate whether the change in settlement fees is within the tolerance. The quantities are provided to settlement agents by the GFE, so training will be much less involved. Assuming four hours of training at an opportunity cost of $72.12 per hour (based on a $150,000 fully-loaded annual salary); tuition of $250 per worker for small firms and a discounted tuition of $125 per worker for large firms; and that half of the workers in small firms and one quarter of the workers in large firms require training; then the total cost of training is $71 million, of which $62 million is borne by small business.

Recurring Costs of the New HUD-1

There are few recurring costs associated with the revised HUD-1. The revised HUD-1 will very likely have fewer entries than the existing HUD-1 which will require fewer explanations of figures than is true with the existing forms. This is because of the combined subtotals presented in many sections in the new GFE in lieu of the frequently numerous broken out individual fees that we see on the GFE. The same is true when comparing the revised HUD-1 to the existing HUD-1. Comparing the new GFE to the revised HUD-1 should be simpler than in the past because it will be much easier to find entries on the new HUD-1 that correspond to the new GFE because they have the exact same description. And, of course, there are fewer entries to deal with. It is hard to imagine how simpler forms could be more costly to explain to borrowers.

There may be recurring costs from the addition of the comparison page (page 3) of the HUD-1. This new page will serve two purposes: 1) as a crosswalk between the HUD-1 form and page 2 of the GFE and 2) presenting a summary of the loan terms similar to page 1 of the GFE. The costs of completing this page are minor. For originators it could be close to zero. Although the lender has to provide the settlement agent with information on the loan terms and some of the loan settlement charges, it should not constitute an additional burden. First, if the loan originator used a software program to generate the GFE, he or she would already have entered those data. A typical software program would print a HUD-1 for an originator that would contain all of the required data concerning loan terms and settlement costs. The only information that is not already there is information concerning the escrow account. Second, transmitting the information on page 3 to the settlement agent will not constitute an additional burden

either: lenders and brokers already send documents to settlement agents, the cost of an additional page will not be noticeable. However, there may be a small burden in certain cases, and so we assume that the average burden is ten minutes per loan.

Settlement agents may also face an additional burden, although this is not likely either since the lenders are responsible for providing the data. The settlement agent may have to fill out the form if the lender does not transmit it on a completed HUD-1 page 3. The settlement agent may also want to check the information concerning settlement costs, tolerances, and loan terms to make sure they agree with the GFE. In some cases, the settlement agent will have to calculate the tolerances. Preparing page 3 of the HUD-1 may also alert the settlement agent to inconsistencies that would not have to be resolved before closing. Thus, although the addition of this page may have a very small impact, we assume that it will add five minutes on average to the time it takes to prepare a settlement. Taking loan originators into account, the total time burden is fifteen minutes per loan. The compliance cost of the change to the HUD-1 for the industry as a whole is thus $18 per loan (fifteen minutes at $72 per hour[57]). The recurring compliance cost to the industry would be $225 million annually ($18 per loan X 12.5 million loans annually), of which small business would bear $107 million annually. During a high-volume year (15.5 million loans annually), the annual recurring compliance cost of the HUD-1 would be $279 million annually.

[57] As for the GFE, an alternative method could be used to generate an estimate of the opportunity cost of time spent on a script. Instead of assuming a $72.12 opportunity cost (from a $150,000 fully-loaded salary), one could construct a cost estimate from industry-specific data. For example in Tucson, Arizona, the cost of labor (compensation and benefits) of a Real Estate Clerk is $16.66 per hour and $74.61 per hour for a Real Estate Attorney.

The benefits of the comparison page of the HUD-1 are not estimated separately from the benefits of the new GFE ($6.48-$8.38 billion, see Section I.B of Chapter 3). It is assumed that page 3, which displays tolerances and loan terms, reinforces the consumer savings of the new GFE by compelling settlement agents and borrower to check the compliance with the tolerances. The comparison page is a vital part of the reform. Requiring it is expected to increase the number of consumers who realize the full benefits of the final rule. The benefit of the comparison page is to double-check the final figures.

Changes in the Final Rule to Reduce the Regulatory Barrier of the HUD-1

Recurring Costs of the HUD-1 Addendum

Comment. Many comments were opposed to the proposed HUD-1 Addendum or "script" of the 2008 proposed rule. The purpose of requiring settlement agents to complete and read this form document was to have them describe, at settlement, the terms of the loan and to compare the settlement charges on the GFE to those on the HUD-1. The primary objection to the script was the time costs. HUD estimated the worst case scenario of the added time required of a non-conscientious agent dealing with a very complicated loan product to be an additional 45 minutes. We assumed that the script would lead to an additional thirty minutes preparing the script, and an additional fifteen minutes to the actual closing procedure consisting of five minutes reading the script, and ten minutes answering questions. To be cautious, we applied this estimate to establish the outer bound of the opportunity cost of the closing script to the settlement firm at $54 per settlement. The total cost of the script in a normal year (12.5 million originations)

could be $676 million. Settlement industry groups were concerned about the potential additional costs of preparing and reading the script.

A second objection is that the script could place a settlement agent in the position of committing the unauthorized practice of law. This would occur if they were required to answer questions concerning issues such as the loan terms for which they had no responsibility.

Response. At recent roundtables, representatives of the settlement industry have assured HUD that their primary goal is transparency and customer service. HUD assumed that without the script settlement agents would neither take any time to explain the HUD-1 to borrowers nor take any time to answer questions. Thus, HUD's cost estimate of the script may be exaggerated. In the world of the conscientious settlement agent, the additional burden of the script at closing would be closer to zero. However, because of the concern expressed concerning the implications of the potential cost and legal implications of the script, HUD will not require a script in its final rule.

To replace the script, HUD has added a page to the HUD-1 form. This will contain much of the same information but will much easier to fill out and will not have to be read the settlement agent. The top half will contain a table that compares settlement charges with those on the GFE and shows the amount and percentage by which the charges have changed (in order to check whether the change is within the tolerance). The bottom half of the page consists of a summary of the loan terms, very similar to the first page of the GFE.

The impact of this change is to reduce the maximum additional time imposed, which is expected to be imposed by the rule, from 45 minutes to 15 minutes per loan. At

an opportunity cost of time of $72 an hour for industry, this translates to a decrease in the regulatory burden of $36 per loan, or $450 million over an expected 12.5 million loans.

Difficulty Comparing the New GFE and HUD-1

Under the March 2008 proposed rule, the current HUD-1/1A Settlement Statements would have been modified to allow the borrower to easily compare specific charges at closing with the estimated charges listed on the GFE. The proposed changes would have facilitated comparison of the two documents by inserting, on the relevant lines of the HUD-1/1A, a reference to the corresponding block on the GFE, thereby replacing the existing line descriptions on the current HUD-1/1A. The proposed instructions for completing the HUD-1/1A would have clarified the extent to which charges for individual services must be itemized. The script was proposed to facilitate the comparison.

Many commented that borrowers would require more help in comparing the new GFE to their HUD-1. Lenders, mortgage brokers and title and closing industry representatives generally stated that the HUD-1 should be in the same format as the GFE to enable comparisons of estimated and actual charges. A lender association stated that the proposed changes to the HUD-1 fall short of making the GFE and HUD-1 correspond. Lenders also stated that the proposed HUD-1 is not consistent with the disclosures mandated by TILA.

A consumer group stated that while referencing the GFE lines on the settlement statement is an important step, HUD should mandate a summary settlement sheet that corresponds exactly to the summary sheet of the GFE. According to this group, this would obviate the need for a crosswalk between the GFE and the settlement statement.

The consumer group stated that the HUD-1 should be easily comparable to the GFE and should facilitate, rather than hinder TILA and HOEPA compliance.

One broker suggested that HUD had created three different documents--the GFE, the HUD-1 and the Closing Script—that present the same information in completely different formats, and this will add to costs and confusion.

HUD agrees with the many commenters who pointed out the importance of comparability between the GFE and the HUD-1. The main strategy for facilitating comparability between the GFE and HUD-1 will be by inclusion of a new third page comparison chart with the HUD-1. This will clearly present whether settlement fees are within the tolerances on the top half of the page and will present a description of the loan in a similar fashion to the GFE on the bottom half.

The final rule provisions for describing some loan terms in the page 1 of the GFE and page 3 of the HUD-1 are similar to the Truth in Lending Act (TILA) regulations, however the differences in approach between the TILA regulations and HUD's RESPA rule make them more complementary than duplicative. The TILA and RESPA approaches to mortgage loan terms disclosure are most similar when the loans are very simple, e.g., fixed interest rate, fixed payment loans. The approach differs for more complex loan products with variable terms. In general, TILA describes how variable terms can vary (e.g., the interest rate or index to which variable interest rates are tied, how frequently they can adjust, and what are the maximum adjustment amounts, if any), but forecasts the "likely" outcome based on an indefinite continuation of current market conditions (e.g., the note rate will be x in the future based in the index value y as of today). The RESPA disclosures in the GFE and HUD-1 comparison page focus the

borrower on the "worst case scenario" for the loan product to ensure borrowers are fully cognizant of the potential risks they face in agreeing to the loan terms. The disclosures on the GFE are meant to be as simple and direct as possible to communicate differences among loan products. HUD's approach to these disclosures thus supports consumers ability to shop for loans among different originators. For a given set of front-end loan terms (initial interest rate, initial monthly payment, and up-front fees), originators have an incentive to offer borrowers loans with worse back-end terms (e.g., higher maximum interest rate, higher prepayment penalty) to the extent capital markets are willing to pay more for loans with such terms. While brokers are required to disclose such differentials on the GFE and HUD-1, lenders are not. HUD's GFE will help consumers to quickly and easily identify and distinguish loan offers with similar front-end terms, but worse back-end terms, while shopping for the best loan. Requiring a comparison page will act to double-check the HUD-1 and thus enhance the realization of the benefits of the simpler GFE.

Efficiencies and Reductions in Regulatory and Compliance Burden

Efficiencies come from time saved by both borrowers and originators as a result of forms that are easier to use, competitive impacts in the market, the decrease in the profitability of searching for victims, and the decrease in discouraged potential homeowners. All these are ongoing as opposed to one-time costs. The value of time saved for borrowers is $1,169 million and for industry $1,166 million (the sum of time saved answering borrowers' questions and from the simplicity of average-cost pricing). There are also positive spillovers of increasing consumers' level of awareness. First, consumers will be less susceptible to predatory lenders and therefore this type of wasteful

activity will be discouraged, freeing up resources for more productive purposes. Second, by better understanding the loan product, there will be a decrease in the probability of default leading to foreclosure, which can dramatic social costs.

Shopping Time Saved by Borrowers

Consumers will save time in shopping for both third-party services and mortgage loans as a result of the new GFE. HUD expects that the time savings for consumers will counterbalance some of the costs imposed on industry. The increased burden on originators of arranging third-party settlement services is likely to be much more than offset by a reduction in the aggregate shopping burden for third-party providers incurred by borrowers. Originators will be highly motivated to find low third-party prices. Originators could pass the savings on and make it easier to appeal to borrowers, or alternatively, could raise their origination fee by the savings in third-party fees and earn more profit per loan. Or the final result could fall somewhere in between the two. Regardless of which path any originator chooses, the lower third-party prices work to his or her advantage; originators will probably be aggressive in seeking out lower prices.

The borrower benefits to the extent that, upon receipt of the GFE, he or she immediately has good pricing information on third-party services. The borrower could immediately decide to use the originator's third parties, in which case his or her search is over. Or, the borrower could search further with the originator's prices as a good starting point and available as a fall-back, in which case the borrower's search efforts are likely to be greatly reduced. In both cases the borrower searches less, but spending less time searching does not imply less benefits from the search.

The final GFE also creates time efficiencies by making mortgage loan details more transparent to consumers. Shopping will be encouraged because consumers will have an easier time understanding and comparing loans with a standard and comprehensible GFE. The final rule increases the amount of information processed by consumers; shopping accomplished; and the benefits realized from doing so.

It is possible that under the final rule that some consumers will want to spend more time searching. Although additional time spent searching reduces the time spent on other activities such as leisure, the reward of search is an increase in consumer savings. Assuming that the GFE increases the productivity of every hour of search, it therefore also increases the relative opportunity cost of leisure. Consumers will spend more time shopping to receive additional income. Under these circumstances an increase in the time spent shopping does not constitute a burden imposed by the rule since the increase in time is voluntary. Consumers are free to remain at previous lower levels of shopping and enjoy a lower increase in saving from the rule.

We do not expect the average consumer to spend more time searching because there are other effects that should dominate the incentive described above. First, the higher productivity in search of the new GFE increases a consumer's savings at all levels of search: consumers will be able to reduce their level of effort and retain the same level of saving previous to the rule.[58] Second, we expect that a large portion of the increase in savings will be independent of an individual's shopping behavior. As the market

[58] These effects are equivalent to the income and substitution effects of consumer theory to understand the effect of a price change on the consumption of a good. In this case, the increase in productivity of shopping should be considered as reduction in the price of savings in terms of leisure. The income and substitution effect move in the same direction for the normal good whose price has changed but the opposite directions for the substitute.

becomes more competitive, shoppers who are less sophisticated or less diligent may still benefit from the competitive pressure of others' shopping. This additional saving will allow consumers to spend less time searching. The time that they do spend searching, however, will be more effective and lead to greater savings. The new GFE will allow consumers to spend more time comparing and evaluating offers and less time trying to decipher the loan details.

Given that consumers will reduce the time spent searching as a result of this rule, then we would be underestimating the benefits to consumers by only counting the gain in income from reduced fees and not the gain in time saved. Considering the number of loans the average originator closes per year, the aggregate decrease in search efforts by borrowers is very likely to exceed the increase in aggregate search effort by the originators. For example, if each borrower saves an average of 15 minutes in shopping for third-party services, then the total savings to borrowers would be $234 million.[59] As discussed Sections VII.E.1 and VII.E.2 on tolerances, the new form and the tolerances will enable borrowers to save time shopping for loans and for third-party settlement service providers. If the new forms save the average applicant one hour in evaluating offers and asking originators follow-up questions, borrowers save $935 million.[60] The

[59] Calculated as follows: 21,250,000 projected mortgage applications (see Chapter 2) times $44 per hour times 0.25 hour (or 15 minutes) gives $233.750 million. The $44 per hour figure is based on the average income ($92,000) of mortgage borrowers, as reported by HMDA; the $92,000 income figure is divided by 2,080 hours to arrive at the hourly rate of $44.23 or $44. If the borrower saved 30 minutes in shopping time, then the total savings would be $468 million.

[60] Calculated as follows: 12,500,000 loans times 1.7 applications per loan times 1 hour per application times $44 per hour, the average hourly income of loan applicants ($92,000 per year/2080 hours per year). See earlier footnote.

total value of borrower time saved shopping for a loan and third-party services comes to $1,169 million.[61]

Time Saved by Originators and Third-Party Service Providers

Originators and third-party settlement service providers will save time as well. If half the borrower time saved in (1) above comes from less time spent with originators and third-party settlement service providers, then originators spend half an hour less per loan originated answering borrowers' follow-up questions and third-party settlement service providers spend 7.5 minutes less with borrowers for a saving of $765 million[62] and $191 million, respectively, for a total of $956 million.[63]

Time Saved from Average Cost Pricing

As discussed in Chapter 3, the final rule allows pricing based on average charges. This reduces costs because firms do not have to keep up with an itemized, customized cost accounting for each borrower. This not only saves costs when generating the GFE, it is also saves quality control and other costs afterwards. Industry sources have told HUD that this could be the source of significant cost savings.

As explained above, there will be reductions in compliance costs from average cost pricing. It is estimated that the benefits of average cost pricing (e.g., reduction in the

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[61] The benefits are calculate using the ratio of 1.7 applications per loan, which is a measure of the current state of affairs. Although we calculate administrative costs for firms at different ratios (1.7 and 2.7), it would be misleading to calculate consumer benefits at higher ratios. Going from an average of 1.7 to 2.7 applications per loan does not save the average consumer more time. It is clear that the consumer will not be harmed because the increase in applications is voluntary but should not be counted as an efficiency. As argued in the text, we believe that the net change in time spent searching will be negative.

[62] Calculated as follows: 12,500,000 loans times 1.7 applications per loan times 0.5 hours per application times $72 per hour, the average hourly income of loan originators ($150,000 per year/2,080 hours per year).

[63] Just as we do for consumers, we estimate the value of time efficiencies using the 1.7 application per loan ratio even when comparing it to costs generated using the higher 2.7 ratio. It would not be logical to claim that we are saving a firm any time by requiring them to process additional applications. However, it may be sensible to reduce the recurring compliance costs from assuming a higher number of applications because the additional application will not be as much of a burden as it was before.

number of fees whose reported values must be those specifically incurred in each transaction) will lead to a reduction in originator costs of 0.5 percent, or $210 million. No breakdown of fees is needed. No knowledge of an exact fee for each specific service needed for the loan is required for the GFE. In addition, no exact figure for the amount actually paid needs to be recorded for each loan and transmitted to the settlement agent for recording on the HUD-1. The originator only needs to know his or her approximate average cost when coming up with a package price that is acceptable. The cost of tracking the details for each item for each loan is gone.

Social Efficiencies

In this section, we discuss two social efficiencies of the rule: the reduction of non-productive behavior and positive externalities of preventing foreclosures.

Reduction in Non-Productive Behavior

By reducing the profitability of searching for less-informed borrowers, the rule will lead to a more efficient allocation of resources.

The primary benefit to consumers is the transfer of surplus from firms that charge significant markups. Much of the excess fees earned by loan originators and settlement firms is extracted costlessly. Price-discriminating firms are able to assess the information asymmetry between themselves and potential borrowers and estimate the consumers' willingness to pay a markup beyond the costs of originating a loan. Most loan originators base their estimates of a consumer's level of information on signals form the consumer. They do not need to expend additional time or resources to do so. However, there is a minority of loan originators that devote significant resources to advertising to borrowers with a lower expected level of financial sophistication. If the rule leads to a reduction in

predatory behavior, there will be a gain in social welfare equal to the costs of actively searching for less informed borrowers.

The loan originator acts to maximize his or her expected profit. By raising the requested settlement charges above the settlement costs, a loan originator increases his or her mark-up but increases the probability that the consumer will reject the offer. The extent of a consumer's knowledge of the market will also raise the probability of rejecting a markup. The optimal markup is the one at which the net revenues from offering loans at higher prices and a higher rejection rate equals the net revenues from offering loans at lower competitive prices and a lower rejection rate. It is expected that the rule will increase the average individual's information; increase the likelihood that they would reject excessive fees; and thus reduce the prevalence of high markups. This reduction is what constitutes the transfer to borrowers of $668 per loan.

An aggressive seeker of fees may choose to actively search for less informed borrowers who are more likely to accept loans with excessive fees. The optimal level of search effort is the one at which the marginal cost of searching is equal to the change in probability of acceptance from finding less informed clients times the markup (marginal benefit of search). By increasing the level of information among consumers, the rule will raise the marginal cost of searching for vulnerable borrowers and thus will lead to a lower optimal level of searching by loan originators.

Whenever producers expend substantial effort to extract consumer surplus, there is a deadweight loss. The predatory lender diverts resources from producing output to producing markups (consumer loss). By creating transparency and enhancing consumer's understanding, the rule will not only lead to transfers of excess fees to

consumers but will inhibit costly predatory behavior. Reducing this activity will lead to a net gain in social welfare equal to the sum of the marginal costs of extracting the markup.

The total transfer to consumers of $5.88 billion represents 14 percent of the total revenue of originators, which is projected to be $42.0 billion. As explained above, this gain in surplus is greater than the loss to producers when firms are engaged in wasteful predatory behavior. If the decline in this activity represented one percent of current originator effort, this would result in $420 million in social surplus. In the absence of this activity, these resources could be devoted elsewhere making society richer. The transfer to consumers is composed of both the lost excess profits from markups and the deadweight loss from the inhibited predatory activity to achieve those markups. Thus, the gain to consumers will outweigh the loss in profits of predatory firms.

External Benefits of Preventing Foreclosures

Another social benefit of the rule is its contribution to sustainable homeownership. It is more likely that consumers who understand the details of their loans will avoid default and thus foreclosure. There are two ways in which this rule will contribute to sustainable homeownership. The first is to encourage shopping by providing a transparent disclosure of settlement costs and other loan details. Such competitive market behavior should reduce settlement costs and provide a small cushion for borrowers in the eventuality of financial distress. The second is by educating consumers and helping them choose the loan that is most appropriate. A better understanding of the loan details should lead to a better understanding of the risks inherent in assuming a large financial obligation, and thus a better decision by the borrower as to the best loan or even whether homeownership is the optimal choice.

Factors that precipitate default are downward trends in property values, a loss of income of the borrower, and an increase in interest rates for borrowers with adjustable-rate mortgages (ARMs). None of these events can be predicted with certainty and understanding the loan itself cannot eliminate the uncertainty. However, a full appreciation of the potential risks of the loan should lead to a careful decision as to whether the loan vehicle is the best one given the uncertainty. For example, knowing how high your interest rate and monthly payments can go should make the loan applicant hesitant to accept an ARM unless the borrower has the income security to do so. Given the same information, different borrowers may choose different loans depending on their risk and time preferences. However, it is important that they make an informed decision.

There is strong evidence that borrowers underestimate the costs of adjustable rate loans. Buck and Pence (2008) assessed whether borrowers know their mortgage terms by comparing the distributions of these variables in the household-reported Survey of Consumer Finances (SCF) to the distributions in lender-reported data. The authors find that although most borrowers seem to know basic mortgage terms, borrowers with adjustable-rate mortgages appear likely to underestimate or to not know how much their interest rates could change. Borrowers who could experience large payment changes if interest rates rose are more likely to report not knowing these contract terms. Difficulties with gathering and processing information appear to be a factor in borrowers' lack of knowledge. The final GFE would present critical loan terms such as the maximum monthly payment on the first page in order to better inform borrowers.

The least desirable consequence of an uninformed decision is foreclosure. The Joint Economic Committee of the U.S. Congress estimates the total costs to society at

close to $80,000 per foreclosure. The foreclosed upon household pays moving costs, legal fees, and administrative charges of $7,200. A study from the Federal Reserve Bank of Chicago reported that lenders alone can lose as much as $50,000 per foreclosure. Standard and Poor's describes these costs as consisting of loss on loan and property value, property maintenance, appraisal, legal fees, lost revenue, insurance, marketing, and clean-up. Of these costs, the primary cost to lenders is the cash loss on property.

The lender and borrower are not the only parties to suffer from a foreclosure. It is often argued that there are negative impacts to the value of neighboring properties from a foreclosure. There are many reasons for these externalities. There is an amenity value to having an up kept property next door; foreclosed properties if vacant can attract crime; and there may also be a depressing effect on the local economy. A reasonable estimate of the negative externality of a foreclosure on nearby properties is $1,508. In addition, the local government loses $19,227 through diminished taxes and fees and a shrinking tax base as home prices decrease. The total benefits of preventing a foreclosure is $77,935 in averted costs. It is difficult to estimate how many foreclosures a uniform and transparent GFE with settlement fee tolerances would prevent. However, preventing 1,300 foreclosures nationwide would yield $100 million of benefits.

Other Efficiencies

There are other potential efficiencies that are anticipated from the new GFE approach but would be difficult to estimate. For example, studies indicate that one impediment to low-income and minority homeownership may be uncertainty and fear about the home buying and lending process. The new GFE approach should increase the certainty of the lending process and, over time, should reduce the fears and uncertainties

expressed by low-income and minority families about purchasing a home (see Section VII.F of Chapter 3). As discussed in Section IV.D.4 of Chapter 2, improvements in lender information (e.g. interest and settlement costs) should also lend to a general increase in consumer satisfaction with the process of taking out a mortgage (see CFI Group, 2003).