

# Full Description — MBA Options for RESPA Reform



## Introduction

The Mortgage Bankers Association (MBA) is asking its members to comment on three options for Real Estate Settlement Procedures Act (RESPA) reform. These options were developed by a task force representing a cross section of MBA members under the leadership of MBA Chairman Regina Lowrie, in response to indications that the Department of Housing and Urban Development (HUD) intends to go forward with RESPA reform.

## Threshold Determination

The threshold determination for consideration by HUD is whether it should go forward with reform at all through rulemaking or let the market proceed as it has been in reforming itself. MBA has long supported improvement in the mortgage process for consumers. However, MBA believes there are compelling cost and other considerations, also in the interests of consumers, that might lead HUD to conclude that it should forego RESPA reform through rulemaking. HUD would then let the market continue to operate, innovate and simplify the mortgage process under the current rules.

Last year, following the withdrawal of HUD's reform proposal, approximately 15 million mortgage loans were settled under the current RESPA rules. Since RESPA was enacted in 1974, hundreds of millions of other transactions have been carried out and homeownership has grown to unprecedented levels. While borrowers may gain a greater understanding of the mortgage process as a result of changes in the current system, under the current rules, competition and innovation in the mortgage market are resulting in greater transparency and lower costs to consumers. Any changes to the disclosure requirements, on the other hand, would necessitate spending an estimated one billion dollars in training and systems' retooling costs by almost 10,000 lenders as well as many thousands more loan correspondents and mortgage brokers. Such changes would also cause a high degree of confusion absent the expenditure of hundreds of millions of dollars for consumer education. These costs would ultimately be borne by the very consumers who the changes are meant to serve.

If HUD chooses to revise the current rules, it could pursue one or more of the following options. These options, though costly to implement, would serve the interests of making the mortgage process more transparent and efficient and foster innovation to

lower costs for consumers. Under MBA's proposal, HUD could choose to implement Option 1 — revising the forms and attendant requirements — without implementing the other two options. If HUD seeks broader reform — including the imposition of tolerances — it could implement Option 1 along with Option 2, or Option 1 along with both Options 2 and 3. The options are described below.

## Options

### Option 1 — Improving the Forms and Making Related Changes in the Rules.

Under Option 1, the new GFE would become a standard one-page form that would be provided nationally in all RESPA-covered mortgage transactions. It would:

- Describe that the GFE is an estimate, that it is arrived at based on information provided by the borrower and that it is conditioned on the borrower and property qualifying for the loan;
- Describe the characteristics of the particular loan — amount, term, whether it is FHA or conventional, whether it has prepay provisions, balloon or interest only features;
- Describe the interest rate, APR, discount points and estimated monthly payment;
- Disclose all settlement charges for the mortgage in nine major categories including lender origination charges, mortgage broker origination charges, credit, valuation and inspection charges that are excluded from the finance charge and APR for purposes of TILA, title charges, government recording and transfer charges, interest and mortgage insurance charges, flood and hazard insurance charges, escrow charges, and other mortgage loan settlement charges (such as life-of-loan flood services) that are included in the finance charge; and
- Disclose the maximum amount of any lender payments to mortgage brokers (ordinarily Yield Spread Premium (YSP)). Also, in the interest of facilitating both consumer understanding and fair competition, the form advises that: only mortgage brokers are required to disclose any payments from lenders when they arrange loans; that the YSP should not be used for comparison with lender loans; and borrowers should compare the rate, points and settlement costs of similar loans (as well as the APR) when they shop.

The new HUD-1 would mirror the GFE in disclosing final charges for the same cost categories.

### Benefits of these Changes

- These steps alone would make the settlement cost disclosure process much more comprehensible and useful to consumers.
- The new GFE would tell borrowers what they need to know to shop and compare various loan offers.
- Because the GFE would be easily comparable to the HUD-1, both forms would empower borrowers to determine whether the final charges at settlement bear a reasonable relationship to the estimated costs in the GFE.
- By disclosing costs by major cost categories, rather than itemizing each and every sub-charge on both the GFE and HUD-1, the new forms would stem the proliferation of “junk” fees and market competitors would have to present their best price for each cost category, facilitating competition to lower costs.
- By separating charges that are included in and excluded from the finance charge, both forms would make it easier for industry, consumers and others to calculate the finance charge and the APR.

### Required Regulatory Changes

HUD’s rules would require revision so that the new GFE and new HUD-1 would:

- Be used in all transactions covered by RESPA with the new GFE required at time of application and the new HUD-1 at settlement.
- Disclose totals for each of the nine categories of costs on both the GFE and HUD-1 rather than by separately listing each and every charge on either the GFE or the HUD-1.
- Not separately list each charge that is Paid Outside of Closing (POC) on the GFE form. Instead, require that such charges be included in the category totals and then subtracted from the gross amount to determine the amount required from the borrower at settlement and disclosed on the GFE and on the HUD-1.

For the new GFE, the rules also would:

- Provide that a loan originator could require the information it deemed necessary to issue a GFE to a borrower and the

rules also might offer an optional one-page shopping form for use by loan originators at their discretion;

- Not require the inclusion of any information about required service providers on the GFE. To the extent any information on required providers is necessary, it will be provided on a separate, simpler required provider disclosure.

Also, to effectively implement the new rules:

- A reasonable implementation period of one year is essential to make needed system changes and provide training for the new GFE and HUD-1 forms.
- The HUD Special Information Booklet must be revised to explain the new forms and their use, as well as the categories of settlement charges.
- Necessary consultation with the Federal Reserve should be completed prior to implementation to assure that the Board’s guidance concerning the TILA is consistent with HUD’s changes, including any requirements for TILA disclosures or calculation of the finance charge and APR.
- HUD should act to preempt state laws that conflict with the changes implemented, including any inconsistent disclosure laws, to assure consumers enjoy the greater protections offered by these changes.

### **Option 2 – Establishing Tolerances for Lender and Broker Charges and Making All Categories of Charges More Realistic Estimates.**

- Under this option, in addition to the changes in Option 1, reasonable tolerances would be established for loan originator (lender and mortgage broker) charges. Under these tolerances, loan origination charges (except discount points when borrowers “float”) could not vary by more than 2 percent from the time the GFE is given until settlement as long as the borrower and property qualify for the loan and the borrower does not request a change in the loan described in the GFE.
- To make these tolerances workable and to provide simpler, clearer, figures for all cost categories, as well as to make them supportable under HUD’s RESPA authority, a limited Section 8 exemption would be provided to loan originators and other settlement service providers. The exemption would permit average-cost pricing of all cost categories, as defined in the final rules, and relief from interpretations of Section 8(b) of RESPA as defined in the final rules.

- Moreover, to make the tolerances workable, the rules would establish reasonable remedies if the tolerances are exceeded or the new rules are not otherwise satisfied by the party (lender or mortgage broker) whose fees exceeded the tolerance.

## Benefits

- Borrowers would not confront any unreasonable increases in lender or mortgage broker charges at settlement from those originally offered in the GFE, as long as the borrower and property qualify for the loan specified in the GFE and the borrower does not request a change prior to settlement.
- The provision of a limited exemption for average-cost pricing and from Section 8(b) would result in clearer, more transparent costs to consumers in all categories of charges, which in the case of variable charges would be reduced through competition.
- Reasonable remedies, including a right to cure, would avoid unnecessary litigation that would increase costs to consumers.

## Needed Regulatory Changes for Option 2

HUD's rules would be revised so:

- A 2 percent tolerance would be established for loan originators' (lenders' and mortgage brokers') charges, including any YSP from the time the GFE is given to the time of settlement, provided, the borrower and property qualifies for the loan and the borrower does not request a material change in the loan prior to settlement;
- The GFE would be open for acceptance for a minimum period of at least five calendar days;
- While the GFE would be given based on credit and/or other readily available information, it would be conditioned on final underwriting, concluding that the borrower and property qualified for the loan and that the borrower did not request a material change in the loan;
- Loan originators (lenders and mortgage brokers) would receive a limited Section 8 exemption for average-cost pricing of their own charges and the other categories of costs on the GFE as long as:
  - The overall amount for lender and broker charges at settlement is no greater than the amount on the GFE plus the tolerance, provided the borrower and property qualifies for the loan and the borrower does not request a material

change in the loan prior to settlement; and,

- The charges for each of the cost categories are generally (more than 80 percent) attributable to the sub-items of costs described in the category.
- Loan originators and others also would receive an exemption from Section 8(b) of RESPA concerning mark-ups of third party costs as long as the charges in each cost category are disclosed on the new GFE and HUD-1 and the tolerances are satisfied.

Where the tolerances are exceeded, the rules would:

- Allow prompt, non-judicial, corrective action by the originator (lender or mortgage broker) whose fees exceeded the tolerance to repay any overcharge with the amount due the borrower to increase if the originator does not repay within a fixed period;
- Include a one-year statute of limitations as provided by RESPA for a borrower to bring suit. The statute of limitations would begin to run at the end of the cure period or from an earlier date that the claim is denied and the borrower notified;
- Not provide any right of rescission of the loan based upon an excess of charges over the tolerances; and
- Not apply the tolerances where the borrower or property does not qualify for the loan or the borrower requests a material change in the loan prior to settlement.

## Option 3 – Establishing Tolerances for All Major Settlement Charges Except Government Charges and Pre-Paid Items to Provide Even Better Estimates.

Under this option, in addition to the changes in Options 1 and 2, HUD's rules would be revised to:

- Establish an overall 10 percent tolerance for all third-party costs and title costs. Under this tolerance, the total amount of these charges could not vary by more than 10 percent from the time the GFE is given to the time of settlement as long as the borrower and property qualify for the loan described in the GFE, and the borrower does not request a change in such description.
- Make it possible for loan originators and other settlement service providers to control costs to meet the tolerances and to make the tolerances supportable under HUD's RESPA authority, a limited Section 8 exemption would be provided to loan originators and other settlement service providers. This exemption would permit them to arrange volume discounts to

obtain settlement services without regard to Section 8 along with the exemptions provided under Option 2.

### Benefits

- With tolerances applicable to these cost categories, borrowers would not confront any significant increases in any major vendor costs, as long as the borrower and property qualify for the loan described in the GFE and the borrower does not request a material change prior to settlement.
- Volume discounts, which are legal in other sectors of the economy to lower costs, would be permitted in the settlement services sector to facilitate competition at the wholesale level to lower settlement costs to consumers.
- Cost predictability and competition would more effectively lower costs to consumers than any regulatory controls or monitoring measures.

### Needed Regulatory Changes

- In addition to the provisions above, including a limited Section 8 exemption for average-cost pricing and from Section 8(b), HUD's rules would:
  - Establish a new overall 10 percent tolerance for third party and title costs;

- Provide a limited Section 8 exemption for volume discounts to obtain services that are subject to the tolerances that would provide:
  - As long as the charges in each cost category are within the tolerances on the HUD-1, volume discounts would be permissible to help arrive at such charges, whether or not the charges in such categories are greater than the volume costs negotiated. And, no discount and thus no thing of value, for purposes of RESPA, would be found in any such difference even if the reason for such discounts are based on the delivery of a certain level of business.
  - Not apply the tolerances where the borrower or property does not qualify for the loan or the borrower requests a material change in the loan prior to settlement.

### Conclusion

MBA looks forward to members' input on these proposals. In light of such input, MBA will work with HUD to simplify and improve the mortgage disclosure process to lower costs for consumers. MBA also will meet with various participants in the mortgage and settlement services industries to develop consensus regarding its proposals.



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