June 12, 2008

Regulations Division
Office of General Counsel
Department of Housing and Urban Development
451 Seventh Street, SW
Room 10276
Washington, DC 20410-0001

RE: Real Estate Settlement Procedures Act (RESPA), Docket No. FR-5180-P-01, RIN 2502-A161

Ladies and Gentlemen:

The American Financial Services Association (“AFSA”) appreciates the Department of Housing and Urban Development’s (“HUD”) goal to simplify and improve the disclosure requirements for mortgage settlement costs under the Real Estate Settlement Procedures Act of 1974 (“RESPA”) and to protect consumers from unnecessarily high settlement costs. AFSA is the national trade association for the consumer credit industry protecting access to credit and consumer choice. The Association encourages and maintains ethical business practices and supports financial education for consumers of all ages. AFSA has provided services to its members for over ninety years. AFSA’s officers, board, and staff are dedicated to continuing this legacy of commitment through the addition of new members and programs, and increasing the quality of existing services.

I. Introduction

Observation #1: In the midst of the largest mortgage crisis this nation has faced in decades, resulting in part from inadequate verification of customer-supplied data and inadequate pricing for risk, HUD has issued amendments to Regulation X (herein afterwards referred to as the “Proposal”) that would require all residential mortgage lenders to issue quasi-loan commitments without verification of any of the facts necessary to determine whether the customer has the ability to pay, or is likely to pay, or what are appropriate loan terms.

Observation #2: Everyone involved with consumer credit, regardless of interest, agrees on the need for disclosure simplification. Against that backdrop HUD proposes to quadruple the length of the Good Faith Estimate (“GFE”), revise the HUD -1 Settlement Statement in a way that does not adequately align with the GFE and add a multi-page closing script to the settlement statement, requiring twenty-one pages of explanation on how to prepare it.
Observation #3: The Proposal will create regulatory dissonance for all participants in the mortgage industry, from borrowers to brokers to settlement agents and other vendors and, finally, for lenders. The Federal Reserve Board (“Board”) has issued a lengthy and complex proposed rule which would materially amend Regulation Z. The comment period for that proposed regulation recently closed. The Proposal not only fails to take into account the Board's recent proposed rule, it conflicts with other existing regulations. It appears that very little, if any attempt, has been made to align all the requirements in the Proposal with the requirements of existing law. Experienced practitioners in mortgage law and regulation have informed AFSA leadership that they are at a loss as to how best to guide their clients through the regulatory pitfalls created by the Proposal.

AFSA poses those three observations to illustrate our view that this proposed regulation is profoundly flawed. The bulk of its defects fit within one of three broad categories, namely: (1) the lack of authority under RESPA, (2) the lack of workability in practice, and (3) lack of attention to very critical details—such as carefully worded definitions and addressing readily foreseeable consequences.

A quick example of the first category would be the attempt to force the lender to be bound by the fees and third party charges disclosed in the GFE. HUD has no authority to bind the lender to the disclosed amount of any fee or charge. The name “Good Faith Estimate” was suggested by Congress. The name reflects the statutory intent of the disclosure.

As to the second category, requiring the lender to make any quasi-loan commitment before it is allowed to do any underwriting, seems a bit odd. Further, in some circumstances a lender would not even be able to pull a credit report before being required to issue the GFE. HUD leaves open the question as to whether the proposed GFE application would be a credit application for purposes of the Equal Credit Opportunity Act (“ECOA”) or the Home Mortgage Disclosure Act (HMDA), instead of coordinating with the Board to provide definite guidance on these critical issues. HUD does not discuss FCRA at all in this context. However, if the GFE is not an application under the Fair Credit Reporting Act (“FCRA”), a lender could not obtain a credit report prior to making its binding pricing decision if it takes its application by phone. This is because the FCRA requires written authorization from the customer to pull a credit report when it is not in connection with an application for credit (or one of the other enumerated authorized purposes not applicable here)

The third category is illustrated by the defects in the Proposal’s handling of settlement service pricing reform. This is the only portion of the Proposal that could have had any potential for reducing consumer cost, but this option is unlikely to be utilized because it fails to provide Section 8 protection for parties desiring to utilize discounts or average cost pricing, fails to preempt state law and attempts to outlaw up-charges. These deficiencies make the attempted reforms meaningless.
The Proposal reveals a very limited view of how the mortgage shopping, application, and origination processes actually work today. This narrow view has produced a one-size-fits-none proposal that is rigid, inflexible and at complete odds with the many ways in which consumers shop, applications are submitted and lenders underwrite loans today.

The Proposal would dramatically change the entire mortgage loan application, underwriting and origination process for every lender in the country. Unfortunately, the changes will increase risk for every participant in the origination process and will introduce substantial additional cost to each step of the process. Both effects will translate into higher mortgage costs for all consumers. Additionally, the Proposal fails to recognize the widespread use of risk-based pricing, which has opened the mortgage market to many individuals with less than perfect credit. Risk-based pricing requires lenders to fully underwrite an application before the lender can assign an appropriate price to the application. Risk-based pricing brings mortgage credit within the reach of individuals who would otherwise be denied credit, and the Proposal needlessly jeopardizes that function.

The Proposal would change the GFE into a quasi-loan commitment by establishing tolerances to which a lender is held on most settlement service charges, lender’s fees other than discount points and, upon rate lock, discount points. Furthermore, HUD makes an additional troubling statement in the Supplementary Information Part IV, 73 FR 14035:

“However, borrower’s may not be rejected unless the originator determines that there is a change in the borrower’s eligibility based on the final underwriting, as compared to information provided in the GFE application and credit information developed for such application prior to the time the borrower chooses the particular originator.”

fn 8: “Unforeseeable circumstances resulting in a change in the borrower’s eligibility may also be a basis for rejecting the borrower. . . .”

This suggests that perhaps in HUD’s view, the only permitted function of underwriting is to verify the six pieces of information along with any credit information developed prior to the consumer “choosing” the originator and submitting a mortgage application. Thus, the only basis for rejecting an application would be limited to those six items and perhaps the credit report. This language introduces uncertainty and risk concerning the use of several underwriting factors critical to determining ability to repay, such as monthly debt service, number of dependents, and residual income.

The Proposal would revise both the GFE and HUD-1 without putting either one in a format compatible with the other. It would also completely change and expand the function, duties, and activities performed by the loan closer (as well as increasing their risk) by creating a lengthy “closing script” to be read by the closer at each closing. The Proposal would obscure the disclosure of mortgage broker compensation. This is contrary to the position taken by the Board in its TILA proposal, which would highlight the fees
received by the mortgage broker. The Proposal would also impose new definitions and rules on the required use of settlement providers. The Proposal’s lock-step process seems to be completely unaware of the existence of non-purchase money lending, and in particular, debt consolidation lending in which looking at different solutions and making adjustments as information comes in is the norm. It also appears to assume everyone locks rates.

Due to the dramatic changes proposed, a 12-month implementation period for the GFE will not be sufficient. AFSA suggests that a 24-month implementation period is more realistic, given the extensive nature of the industry re-tooling being called for. Lenders will also have substantial demands placed on resources at the same time by the pending amendments to Regulation Z under the Truth in Lending Act (“TILA”).

HUD structured the proposed changes to encourage mortgage shopping, but does not appear to have spent time on determining whether the proposed changes will result in any additional shopping. HUD states the goal of promoting shopping as justification for the Proposal, yet has provided no research in support of the Proposal on the likely efficacy of the Proposal in achieving that goal. RESPA neither directs nor authorizes HUD to pursue this goal. It would be unfortunate if massive changes were imposed, only to discover they had almost no impact on consumer behavior. Given the public’s wholesale acceptance of the internet for all manner of shopping, and the widespread availability of mortgage information on it, that is an entirely likely outcome.

The Proposal ventures into the territory covered by other regulations, while making no attempt to align the terminology or delivery with the disclosures and rules contained in TILA/Regulation Z, the Home Mortgage Disclosure Act (“HMDA”)/Regulations C, FCRA, and the ECOA/Regulation B. Although HUD conferred with the Board on the Proposal, it conflicts in several regards with the recent Board proposal to amend TILA and Homeownership and Equity Protection Act (“HOEPA”).

In fact, many of the issues that HUD tries to address have already been addressed by the Board’s proposed amendments to TILA. AFSA requests HUD to participate in the Board’s review and revision of mortgage TILA disclosures so that HUD and the Board can promulgate regulations that coordinate RESPA and TILA disclosures. That would provide for a single set of simpler, integrated and streamlined disclosures. Coordinating these changes will provide much more useful and understandable disclosures for consumers and will greatly lessen the costs and compliance burdens created by uncoordinated piecemeal changes.

Along the same line, HUD might consider working with the Board and other agencies charged with portions of the residential mortgage credit governance to create a standing body, perhaps like the Federal Financial Institutions Examination Council (“FFIEC”), to develop mutually consistent regulations, commentary, and guidance on parallel paths. Such collaboration could facilitate development and submission of integrated proposals to Congress for statutory authorization needed to support comprehensive regulatory reform.
II. The Proposal Grossly Exceeds HUD’s Statutory Authority

A. RESPA Neither Envisions, Nor Authorizes Most of the Proposal

There are rules to promulgating regulations. Simply put, the primary rule is that the impact and effect of the regulations may not exceed the parameters of the legislation the regulations support. That is, the scope of the regulations may not exceed the stated purpose of the legislation.

The Congressional intent relative to RESPA is clear. As expressly stated in Section 2, the purpose of RESPA is “to effect certain changes in the settlement process for residential real estate that will result in more effective advance disclosure to home buyers and sellers of settlement costs” and “in the elimination of kickbacks or referral fees that tend to increase unnecessarily the costs of certain settlement services.” That is, the intended purpose of RESPA is to provide advance estimates of settlement costs and to eliminate kickbacks and referrals.

Even if one were to assume that overhauling the entire settlement process would achieve some of HUD’s goals, HUD does not have that authority. The problem is that there is no Congressional authority or evidence of intent for RESPA to be that vehicle. Instead of going to Congress for specific authority to restructure the entire process, HUD assumes the unilateral authority to do so by regulation.

HUD lacks the authority to issue many of the rules contained in the Proposal. The legacy of these regulations is likely to be a tidal wave of litigation which would attack the rules piece by piece, leaving the industry uncertain as to how to discern and comply with those remaining portions judicially determined to be within the scope of authority granted to HUD under RESPA.

In the event of Congressional ambiguity or silence relating to a particular statute, great deference is to be given to the construction placed upon a statute by the agency responsible for its administration. The power of an administrative agency to administer a Congressionally created program necessarily requires the formulation of policy and the making of rules to fill any gap left, implicitly or explicitly, by Congress. It is, however, equally clear that such deference is to be given only in the case of silence or ambiguity on the part of Congress and the agency's interpretation must be based upon a permissible construction of the statute. Administrative constructions, which are contrary to the clear Congressional intent, must be rejected (Chevron, U.S.A., Inc vs. Natural Resources Defense Council 104 S.Ct. 2778). In short, in promulgating regulations which construe and interpret the legislation it administers, the administering agency must respect the Congressional intent as evidenced by, and reflected in, the Congressionally stated purpose of the statute. The agency's reading of the statute may not be “arbitrary, capricious or manifestly contrary to the statute.” Rather, the construction is permissible
only when “the agency's reading fills a gap or defines a term in a reasonable way in light of the legislature's design” (Regions Hosp. vs. Shalala 118 S.Ct. 109).

HUD's purpose in promulgating the Proposal cannot be regarded as being consistent with Congressional intent as evidenced by the stated purpose or as being in accord with legislative design. The stated purpose of this Proposal is much more ambitious than the permissible parameters stated by Congress in RESPA. As stated in the proposed regulations, HUD's purpose in its promulgation is to: (1) reduce settlement costs by means other than statutorily approved elimination of kickbacks and referrals, (2) eliminate certain practices that increase settlement costs, (3) assure that the costs are as “firm” as possible, (4) provide the borrower with definite loan terms as early in the process as possible, and (5) “level the playing field” between brokers and lenders. These stated purposes extend far beyond providing borrowers with advance disclosure of settlement costs and have virtually no connection with the elimination of improper referrals and kickbacks. To the extent that the scope of these proposed regulations clearly extends far beyond the province of RESPA (which is advance notice of settlement costs and elimination of kickbacks and referrals), they may certainly be regarded as “arbitrary” or “capricious” and definitely do not “fill a gap or define a term in a reasonable way in light of the legislature's design.”

HUD has no authority, acting through RESPA, to effect the proposed modifications and alterations to the current consumer lending process and procedures. The clear language of RESPA and in multiple judicial decisions are clearly contrary to several of the stated purposes of these proposed regulations. For example, one stated purpose is to assure that the disclosed anticipated settlement costs are as “firm” as possible. To achieve this purpose, HUD either freezes the settlement costs indicated on the GFE (i.e. these costs may not vary at loan closing from the sum reflected on the GFE) or imposes “tolerances” on the degree to which they may change at the loan closing (i.e. the fees may vary by 10% at closing from the sum reflected on the GFE). These restrictions effectively constitute a guarantee of closing costs, and this is clearly not within the authority of HUD. HUD attempts to address this issue in the Supplemental Information by distinguishing the Proposal from the original RESPA requirements. See 73 Fed. Reg. 14039-40. In doing so, HUD begs the question of whether the Proposal is within the authority granted by RESPA as it stands today. Clearly, it is not.

RESPA clearly states that the GFE may reflect “an estimate of the amount or range of charges ... the borrower is likely to incur ...” (emphases added). The proposed rule effectively guarantees the cost of settlement services. By contrast, the Congressional Record emphasizes the intent that the GFE may disclose a range of charges, rather than exact numerical amounts.

As has been pointed out by various legislative historians the original enactment of RESPA Section 6 required lenders to disclose the exact amount or, if that was not feasible, a good faith estimate of the amount of each charge. This requirement was found to be sufficiently irrational and illogical that it was repealed the following year when Congress replaced it with the current good faith estimate requirement. The amendment
required the lender to provide a range of charges and specified that the figures provided to the prospective borrowers are to be estimates, and not guaranteed settlement charges.

Finally, to the extent the purpose of the Proposal is to reduce or establish levels for settlement costs, various courts have repeatedly made clear that RESPA is not a price-control statute and was meant to address certain specified practices (i.e. kickbacks and improper referrals), not to enact broad price controls. As several commentators have recounted in a variety of forums, prior to passage of RESPA, a separate bill was introduced in the Senate proposing that HUD be permitted or enabled to establish the maximum amounts of the charges to be imposed upon the borrower and seller for services incident to or a part of a real estate settlement. Congress refused to adopt this explicit price-control proposal. Not only is our interpretation of RESPA’s functions supported by its statutory history, several federal appellate courts have concluded that price control is not among the permitted RESPA purposes. (Kruse vs. Wells Fargo Home Mortgage, Inc., 838 F.3d 49, 2nd Cir- 2004), (Boulware vs. Crossland Mortgage Corp., 291 F.3d 261, 4th Cir-2002). As one distinguished jurist has phrased it, “this would make sense if RESPA were some public utility or other rate regulating statute: it is not.” (Krazlic vs. Republic Title Company, 314 F.3d 875, 7th Cir-2002).

B. The Proposal Conflicts with other Agencies’ Jurisdiction Over Other Consumer Protection Regulations

HUD has no authority to issue regulations that conflict with other federal statutes (ECOA, TILA and HMDA, among others). The decision as to whether an ECOA application for credit has been submitted is a question for the Board to decide. HUD should have consulted with the Board to confirm its view and should have requested that the Board issue coordinated proposed regulations at the same time, with the Board amending Regulation B to define a GFE application in conjunction with the issuance of the Proposal. The coordinated proposed regulations should have clarified whether the GFE application does or does not constitute an application for credit.

Moreover, the entire procedure surrounding the proposed use of the GFE impinges upon the effect and timing of ECOA's and FCRA's adverse action notice (the Proposal forces the lender to make a preliminary approval prior to receipt of a completed application), its procedures concerning counteroffers (the Proposal requires issuance of new GFE for each proposed change in loan terms), and its requirements regarding credit decision notices (it requires underwriting to be complete in a “reasonable” amount of time and rejections to be provided within one business day). They will also interfere with the timing and notice requirements of TILA. Portions of the disclosures on the GFE relating to monthly payments will conflict or be inconsistent with TILA disclosures, and may improperly affect what is deemed to be a reportable application for the purposes of HMDA. Section 226.19 of Regulation Z requires that the TILA early disclosure be given with the RESPA disclosure. It is overstepping boundaries for HUD to dictate when the initial TILA disclosure should be made. Further, the terminology used in the proposed disclosures does not match that used in other disclosures, which will lead to consumer confusion.
HUD takes the position in the Proposal that up-charges by lenders and other service providers are prohibited by RESPA. This position is unsupported by the language of the statute and has been rejected by a majority of federal appellate courts that have addressed the issue.

Additionally, a number of the new disclosures required in the GFE and the closing script are duplicative of the disclosures required by Regulation Z and appear to extend beyond the enumerated purposes of RESPA. Again, the purpose of RESPA, as set forth in Section 2, is to protect consumers from unnecessarily high settlement charges by, among other things, providing advance disclosures to home buyers and sellers of estimated settlement costs and the nature of the settlement process. In addition, Section 5 of RESPA seems to limit the GFE disclosures to information concerning charges for settlement services. Section 5 requires lenders to include with the special information booklet a “good faith estimate of the amount or range of charges for specific settlement services the borrower is likely to incur in connection with the settlement” as prescribed by the Secretary of HUD.1 The purpose of TILA, on the other hand, as set forth in Section 226.1 of Regulation Z, is to promote the informed use of credit by requiring disclosures about its terms and cost. The following disclosures, which are required to appear in the new GFE and in the closing script, seem to be related to the terms of the loan, rather than disclosures related to settlement charges:

♦ The GFE and the closing script would require disclosure of the initial loan balance (loan amount). Section 226.18 of Regulation Z requires disclosure of the amount financed. The disclosure of the initial loan balance is not a disclosure of a “settlement charge.”

♦ The GFE and the closing script would require disclosure of whether the interest rate could rise over the life of the loan. Sections 226.18 and 226.19 of Regulation Z require more comprehensive variable rate disclosures. Again, this disclosure does not relate to settlement charges or the settlement process and is duplicative of TILA.

♦ The GFE and the closing script would require disclosure of whether the loan balance could rise over the life of the loan. Section 226.19 of Regulation Z requires disclosure of negative amortization on certain variable rate loans. Because payment option features are generally offered only on variable rate loans, this disclosure is duplicative of TILA. Additionally, it does not relate to settlement charges or the settlement process.

1 AFSA notes that the Proposal turns this RESPA requirement on its head. In accordance with RESPA Section 5, Section 3500.6 requires that a special information booklet be provided when a lender receives an application for a purchase money federally related mortgage loan. However, the definition of GFE application expressly provides that “[n]either a GFE application nor an application for a prequalification is a mortgage application for a federally related mortgage under this part.” Thus, under the Proposal, rather than being provided with the special information booklet, the GFE is to be provided separately and first, with the special information book to follow only when a mortgage application is submitted.
♦ The GFE and the closing script would require disclosure of any prepayment penalty and any balloon payment. Section 226.18 of Regulation Z requires disclosure of both of these items and the preamble to the proposed rule acknowledges this overlap. These disclosures do not relate to settlement charges or the settlement process and are duplicative of TILA.

♦ The closing script would require disclosure of any late charge. Section 226.18 of Regulation Z requires the same disclosure. This disclosure does not relate to settlement charges or the settlement process and is duplicative of TILA.

♦ The GFE and the closing script would require disclosure of the initial interest rate. Section 226.18 of Regulation Z requires disclosure of the annual percentage rate. The initial interest rate that must appear on the GFE and in the closing script does not duplicate TILA's APR disclosure requirement. In fact, the preamble to the proposed rule makes very clear that the GFE does not disclose the APR. Regardless, these two disclosures are relatively similar. Moreover, presenting consumers two different pieces consisting of similar information, the initial interest rate and the APR, will be confusing for the consumers.

♦ The GFE and closing script would require disclosure of the initial monthly amount owed for principal, interest and any mortgage insurance. Section 226.18 of Regulation Z requires disclosure of payment amounts. The preamble to the proposed rule points out that the monthly payments disclosed on the GFE differ from the monthly payments disclosed on the TILA form because the monthly payments on the TILA form may include taxes. Regardless, this does not appear to relate to settlement charges and is duplicative of TILA. Again, these similar pieces of information will likely confuse the consumer.

♦ The GFE and the closing script would require disclosure of the loan term. While Section 226.18 of Regulation Z does not expressly require disclosure of loan term, it does require disclosure of the payment schedule and the number of payments. Consumers can figure out the loan term from this payment schedule fairly easily and these two disclosure requirements are therefore very similar. Additionally, this disclosure does not relate to settlement charges or the settlement process, which are the enumerated purposes of RESPA.

The increased lender liability for third party fees that change mid-stream may encourage national lenders to contract with only a few national providers who can guarantee price. Similarly, the closing script requirement will likely concentrate business in fewer and fewer closers. The increased risks may well favor the larger, more sophisticated lenders who may be able to more economically hedge against the additional exposures, which would most likely increase the rate of consolidation already evident in the market.

While RESPA, as a disclosure statute, is clearly helpful for consumer shopping, which is one anticipated result of disclosure, nowhere does the law give HUD any authority to govern when or how the lender's own fees must be locked, nor when or how the pricing
of third party service providers must be locked. Yet the proposed GFE would require the lender to commit in the very first disclosure to “1. The interest rate for this GFE is available until ___;” and non-discount points are locked upon issuance of the GFE. To purport to require “quasi-commitments” by attaching locks on fees into the new “GFE application” is not supportable under the law governing Regulation X.

Further, HUD’s venture into underwriting by declaring the conditions under which a lender can turn a borrower down is unsupported by the law. It may run afoul of safety and soundness considerations applicable to depository institutions, and ventures into the OCC’s and FDIC’s venues inappropriately. Finally, there is nothing in RESPA authorizing HUD to mandate when underwriting decisions must be communicated.

III. The Proposal Fails to Reflect the Mortgage Application Processes – Section by Section Analysis of the Proposed Regulation

A. Definitions – Section 3500.2

The Proposal contains new words and phrases that are either undefined or poorly defined, leaving dangerous ambiguity that will lead to enforcement and litigation exposure for lenders. Examples of these new words or phrases are:

♦ “Interest rate-dependent charges and disclosures” – It is unclear what fees and charges are included in this phrase, if points are included in this phrase at all or if points are included in this phrase only if the consumer buys down the rate and whether loan fees are included in this phrase. Additionally, most Regulation Z disclosures are dependent in one way or another on the interest rate—if the rate is changed but all other factors remain the same—the finance charge, total of payments, monthly payment, points, are all probably going to change.

♦ “Final underwriting” – There is no definition of this new phrase; thus, it is unclear how it is distinguished from decisions made in underwriting but before the underwriting process is deemed complete. The lack of a definition leads to a series of questions. Since the Proposal triggers a one day turnaround on notifying the customer of rejection upon completion of “final underwriting,” does a different rule apply for decisions made before final underwriting is complete? Is there a different rule or process applicable if the proposed deal obviously becomes unworkable due to information verification received before “final underwriting” has been completed? Note the likely issuance of multiple rejections during the course of a normal loan application progress through the process, even when an appropriate loan may ultimately be approved. That is a misleading, inefficient, and consumer-unfriendly process to be forced to follow.

♦ “Interest” – This key term is not defined.

♦ “Service Charge” – This term is not defined.
“Upfront Charges” – This term, which is used on the GFE, is not defined.

Furthermore, other terms in the Proposal, while defined, have significantly different meanings in normal lending parlance, leading to consumer confusion. The phrase “credit or charge for the specific interest rate chosen” is one example. This phrase is defined for brokers, only. As applied to lender’s fees, the Supplementary Information seems to include all lender fees in this category, except discount points, but lenders will have to interpret these provisions at their risk, because of lack of clarity.

Finally, the Proposal would change some terms from the meaning they have had under RESPA for many years, making their new meaning vague and subject to litigation. The term “required use” is a good example. The current definition of "required use" in Regulation X means when a consumer must use a certain provider in order to have access to some other particular provider, but does not include the option offering of discounts or rebates for the purchase of multiple settlement services. The Proposal modifies the definition of "required use" to include the use of both economic incentives and disincentives that are contingent on a borrower's use or failure to use a particular settlement service provider.

The resulting "bundling of services" would result in a violation of RESPA's prohibition of required use of certain settlement service providers. However, the Proposal does allow an optional combination of settlement services to a borrower by a settlement service provider when the resulting cost of those combined services is less than the total of the individual cost of those services. Deficiencies in the proposed change of definition include:

♦ The exception is only applicable to fees paid by the borrowers, not sellers. Depending on local custom of who pays for what settlement services, certain settlement services may not qualify for exclusion from the required use definition.

♦ Discounts for the purchase of multiple settlement services can only be offered by a settlement service provider and therefore, will have a major impact on the ability to offer bundled settlement services by builders in exchange for a discounted purchase price.

♦ The proposed definition only carves out an exception to inclusion within the "required use" definition if there is a combination of settlement service fees but does not address the lowering of an individual settlement service fee.

♦ HUD's scheme for bundling disclosure of certain unrelated payments is quite confusing even to experienced practitioners. AFSA believes that it would be difficult for consumers to understand them.
B. Good Faith Estimate or GFE – Section 3500.7(a) – 3500.7(f)

The Proposal would require significant changes to the GFE and the process around providing a GFE. The new GFE form has grown to four pages and contains: a page of information on the proposed loan terms; a page on the settlement costs, broken into groups; a page describing how to shop for a mortgage, which contains a box with the terms of the loan described on the first page, compared to a loan with a lower interest rate and a loan with lower settlement charges, (all of which will need to be calculated and completed); and a page describing the borrower's estimated costs for property insurance, taxes, flood insurance, homeowners association/condominium dues and other costs of home ownership and the application fee, along with a chart for comparison shopping.

HUD does not take into account product availability when requiring to the lender to include disclosures of loans with lower interest rates and loans with reduced settlement charges. Is the lender supposed to include a hypothetical loan that it does not even offer, in order to complete the comparison? If it doesn’t offer such a product, how would it know what terms to fill in? Is simply filling in the alternative as “not available” in compliance with the Proposal in that case?

Instead of providing a GFE upon receipt of a complete application, the Proposal requires a lender to provide a GFE based on the borrower’s name, social security number, property address, monthly income, estimate of property value and loan amount requested (called a “GFE application”). Oral applications must be reduced to written or electronic records and maintained for at least three years.

HUD’s primary motivation appears to be to facilitate comparison shopping between lenders by consumers shopping for a loan. While the Proposal will have severe negative impacts, there has been no research or evidence offered by HUD on whether there is a need for more shopping, nor whether utilizing this plan would result in any additional shopping. AFSA believes that, in this day of the internet, most consumers already have a good idea of the mortgage market before ever contacting a lender or broker, and have no intention of shopping further unless something strikes them as out of line.

Section 3500.7(a)

This section creates a new type of application called a GFE application, which is in essence a request for a good faith estimate. This new application concept is counterintuitive and will create significant confusion. The information the lender can require at this stage is very limited, yet the lender is expected to either provide a binding fee quote that is in essence a mortgage approval or reject the application. If the applicant wishes to proceed with the lender, the applicant may then submit a mortgage application.

The proposed GFE application requires evaluation of the applicant’s credit and eligibility for the loan. Depending upon the circumstances, a GFE application could be a prequalification and/or an application for TILA, ECOA, and HMDA purposes. The numerous references later in the Proposal regarding the refusal to allow a mortgage
application to be submitted or to reject the current application when there are loan changes that affect the GFE quote, probably require lenders to provide adverse action notices under ECOA and report loan denials and new applications on the HMDA LARS report, even though the borrower will be, in essence, continuing with the existing loan application. The result will be distorted loan data with diminished utility for regulators and consumers. If the denial of a GFE application does not trigger ECOA and HMDA then discrimination can occur without being captured, and the purposes of ECOA and HMDA will have been thwarted. Neither alternative is acceptable.

Because the Proposal would require a new application form, new tracking mechanisms would need to be put in place. This prompts a few questions. If the lender assigns a loan number to the GFE form, would that trigger HMDA? If the lender does not assign a loan number, how can the lender store and/or retrieve the data, as the lender is required to do?

The Proposal anticipates the GFE will be issued before the lender has done any underwriting, indeed, before it might be legal for the lender to pull a credit report in many cases (such as telephone contacts). The way the Proposal is written, it appears the lender may not have authority to pull credit at the trigger point for the GFE without first obtaining a written consent from the consumer. The Proposal is unclear as to whether the GFE application is intended to be an application under ECOA or FCRA.

Limiting the amount of information that an originator can require before evaluating the applicant’s eligibility for the loan: (1) prevents the lender from obtaining information needed to provide an accurate fee estimate; (2) requires an originator to make a credit decision without adequate information relating to the applicant’s employment and credit contrary to prudent underwriting practices and current regulatory guidance and requirement; (3) would necessitate the development of new systems that could perform credit analysis based on limited information; and (4) will lead to a significant increase in withdrawn approvals. In fact, the Proposal assumes that lenders can make an assessment of borrowers’ creditworthiness using only a Social Security number, basic income information from the customer, a property address, and the customer’s guess on price/value of collateral (which is often very inflated in today’s market), and their desired loan amount. These complications raise the question, to avoid triggering the GFE applications could lenders consciously collect fewer than all six pieces of information until they complete the full credit application?

Another difficulty with the limiting the originator to the six pieces of information that would trigger the GFE is that originator will not have enough information to identify whether the property the borrower is contemplating buying is commercial, industrial, office, retail, owner occupied dwelling, residential rental, vacation home, condo, purchase money, non-purchase money, first or second mortgage loan. Without that information, the lender does not know whether it makes that kind of loan or not. The programs, underwriting, and pricing differ considerably amongst even the various forms of residential real estate. While the Proposal allows the originator to get the consumer's estimate of the property value and the amount of loan desired, it does not allow the lender to find out what liens are on the property or what the consumer's estimate of the equity is.
This further illustrates the narrow view of the Proposal as to the breadth of the market and the information needed before making even a wild guess at pricing and costs.

An additional problem is that unless the consumer is sitting across from the originator and is willing to wait while the GFE to be prepared, assuming the originator is able and willing to “underwrite,” create, and hand the GFE to the consumer, the originator has no means for providing the GFE to the consumer. The proposed GFE does not require the borrower to give the lender any type of contact information – not a phone number, personal mailing address, or email address. None of these pieces of information may be required by the originator.

This leads to a further reflection. Many, perhaps most, consumers will volunteer some information to enable the originator to provide the GFE to them. If the originator's policy requires the sales person to seek the information, and it is frequently provided, does that not create risk of a claim that the originator violated the law by “requiring” more information than the regulation allows it to require?

It is possible that the originator could start a combined application with the six allowed questions first, then without pause segue into the usual mortgage application questions, in order to get a full application (and have no question about it being an application for credit so a credit report could be pulled). Provided the originator was trained to stop and provide the GFE if the customer objected to proceeding further than the first six questions (subject to all the difficulties noted above), AFSA wonders if this would be permissible under the new regulation.

Alternatively, could the lender have a policy, which it would disclose to the consumer upfront, that the lender will only take an application for a GFE in conjunction with an application for a loan? If the lender could have that policy, it may solve the problem of the lender being required to provide information, such as the interest rate, without key information. However, this approach could hurt consumers who really want to be anonymous while shopping and do not want salesmen calling or unwanted mail.

The proposed GFE process does not appear to consider the needs of borrowers with difficult situations who will not appear to qualify for a loan on a cursory review, but may qualify after the application is worked on. Many customers fall into this category. For instance, assuming a credit report can be pulled, there may be errors in the applicant’s credit report that need to be cleared, examples include: (1) customers with judgments that do not belong the applicant, and (2) customers with excessive debts, but with cash reserves to pay off balance or the ability to prove that the primary borrower on a cosigned loans is performing satisfactorily. Under the proposed process, however, these borrowers may not be able to get past the GFE application stage. No originator will issue a GFE, because these problems are known and there is no way to determine at the GFE stage whether they can be resolved.

The regulation seems to contemplate that a borrower might submit a mortgage application at or about the same time as a GFE application, or at least before the GFE is
required to be provided, but this possibility is not addressed in subsequent parts of the regulation. Is an originator allowed to take the mortgage application at the same time as the GFE application?

*Section 3500.7(b)*

This is the only section in the proposed regulation in which a distinction is made between a mortgage broker and a lender. The Proposal makes significant changes to how mortgage broker compensation is going to be disclosed. The Proposal develops new terminology for disclosure of yield spread premium ("YSP"). Under the Proposal, it is to be referred to as a “credit [to the borrower] for the specific interest rate chosen.” AFSA does not understand what HUD is trying to accomplish with this credit concept. This section is inconsistent with the way that broker compensation currently works.

This section also raises several questions regarding the authority of the mortgage broker. Mortgage brokers do not have the ability to make a mortgage loan or honor a GFE “commitment.” There is no provision for what a mortgage broker is to do if the broker’s GFE is not acceptable to any lender. Does the mortgage broker have the authority to “reject” a GFE application on this basis? If the lender refuses to make the loan on the terms disclosed by the broker has the lender violated the law? Does HUD have the authority to make brokers the agent of lenders for purposes of issuing GFEs that will be “RESPA loan commitments?” How will the broker know what to fill in on the GFE for loan terms, especially, if the broker deals with more than one lender or program? Can the lender issue its own GFE differing from what the broker specified? Does that put the broker in violation of the law? This poses what may be an unacceptable risk for some lenders.

The timing for the lender to provide a correct GFE in a brokered situation is not workable if the lender does not rely on the broker’s GFE, as the lender would be required to provide the GFE within three business days from the date the broker receives the application, notwithstanding when the lender might receive the file from the broker.

HUD seeks to make it clear to the borrower that he/she indirectly pays for the YSP, but it requires a dollar-for-dollar setoff of the YSP against other settlement charges the borrower pays. This eliminates YSP as a means for a lender to compensate the broker for its services.

HUD makes the assumption that the only way for a lender to calculate a compensation payment to a broker is by tying the compensation to the borrower's interest rate. Based on this flawed assumption, neither the new GFE nor Settlement Statement was built to accommodate a lender's compensation payment to a broker based on the loan amount, or a flat dollar amount. The proposed Board’s proposed HOEPA Amendments contemplate such payments, so it is unclear how a lender or broker will comply with both laws simultaneously.
The new GFE and Settlement Statement require that all service charges be lumped together and disclosed on one line, with no way to distinguish those charged by the lender from those charged by the broker; and also no way to distinguish broker charges that are paid for by the lender. AFSA does not believe that hiding either the broker’s or the lender’s fees from the consumer is in the consumer’s best interest. Furthermore, if a lender were to pay broker compensation that is not tied to the interest rate (since interest rate-dependent payments cannot be retained by the broker as described above), there would be no way to disclose the payment without artificially inflating the charges paid by the borrower.

In addition, limiting loan originators to a single service charge does not take into consideration state law restrictions and requirements regarding broker and lender charges. (See Appendix II for examples of state law restrictions and requirements regarding broker and lender charges.)

If payment from the lender to the broker is to be disclosed properly under the new Proposal and forms, the origination fee paid to the broker directly from the borrower is the only remaining means for the broker to be compensated. Unlike today's YSP, such origination fees are finance charges under TILA, and they are also included in the “Points and Fees” definition in state high cost laws. Given the lack of a secondary market for high cost loans, those consumers would likely be shut out of the market if their payment to the broker triggered an HCL law.

Section 3500.7(c)

The Proposal seems to anticipate that there is only one effective GFE at a time. Most lenders do not usually talk about only one option at a time. Lenders talk about features and types of loans, looking to meet the consumer’s needs and preferences. As more information comes in, lenders generally make changes accordingly. It almost seems that any time a lender wants to change anything in regarding the potential loan, the lender would need to provide a new GFE. Is the lender allowed to do this? Often, changes can occur at closing. Would the lender need to provide a new GFE at closing? This would bring the deal back to square one, if it was even possible to provide a new GFE.

The condition that non-interest rate-dependent settlement charges remain in effect until closing should be conditioned on the applicant closing in the time frame established in the GFE. There is no expiration date in the language of the Proposal, but there is a space for an expiration date in the form (#3 under “Important Dates”).

If the GFE applicant fails to submit a timely mortgage application and the originator does not want to be bound to original GFE, the originator is required to either deny the applicant an opportunity to submit a mortgage application or provide a new GFE within three business days. This cumbersome process demonstrates the impracticality of the proposed GFE process. The first option, rejecting the application, is untenable, and the second, providing a new GFE and starting the process over, will frustrate both applicants
and originators. And if a new GFE is provided, what is the status of the “old” GFE application for HMDA purposes? Is it withdrawn, rejected or not accepted?

Section 3500.7(d)

The forms and instructions assume that all lenders lock interest rate, which is untrue. Many do not lock. Others lock on some products, but not on others. As a result of mismatch between the assumption made in the Proposal and reality, the disclosures in the proposed GFE will be confusing or misleading.

The forms and instructions do not take into account the fact that some lenders conduct all or almost all loan origination activities with the customer over the telephone. Many lenders conduct some or all of the taking of the initial loan application by telephone. The Proposal does not specify how to handle this situation. The Proposal also does not discuss web applications and inquiries.

Section 3500.7(e)

It is not clear why government recording and transfer charges are in the “no tolerance” category. These charges can vary based on a number of factors, some of which are not loan-related and are out of the originator’s control, which may or may not be known to the originator at the time the GFE is issued, including:

- Deed recording charges may vary based the number of pages in the deed, which is not prepared by the lender;
- Deed transfer taxes may vary based on the sales price;
- Mortgage recording charges may vary based on the number of pages in the mortgage; although the originator will know the base number of pages in the mortgage and of loan-type related riders, the originator will not have enough information to know whether a condominium or planned unit development (“PUD”) rider will be needed (A review of GFEs shows that this category can legitimately vary greatly between application and closing);
- Mortgage recording taxes may vary based on loan amount or on new money, which will depend upon the payoff balance of the existing lien;
- A power-of-attorney may be used;
- A subordination agreement may be required;
- Lien releases may need to be recorded for unreleased prior liens or judgments; and
- A quitclaim deed may be executed by non-titled spouses in community property states.

The originator is required to notify the applicant within three business days of an increase in charges resulting from unforeseeable circumstances and provide a new GFE, but there is no provision for indicating on the GFE that the information being provided is an update or revision of a prior GFE, so that certain sections of the GFE, such as important dates and applying for the loan will not apply.
Section 3500.7(f)

The requirement that changes in borrower’s eligibility for specific loan terms are to be handled by rejecting the existing loan and issuing a new GFE again is untenable, not in line with borrower’s expectations, and will result in unnecessary loan rejections. ECOA already governs the borrower notification process and originators should be allowed to continue to structure their loan approval, denial, and counteroffer processes in compliance with ECOA. Likewise the requirement to reject the loan application and issue a new GFE when a borrower requests changes to the mortgage loan is untenable.

The requirement that the lender must notify the borrower within one business day of the decision to reject the loan is impractical. Due to the size and scope of lenders’ operations, a lender cannot get a notification out within one day.

Again, as a result of the mismatch between the drafter’s assumptions and reality, the GFE terms lock-down will impede an efficient flow from contact and interest to taking an application (a real application) and getting a preliminary approval.

C. Use of HUD-1 or HUD-1A Settlement Statements – Section 3500.8

The Proposal revises the settlement forms themselves and requires a new closing script process. The proposed HUD-1 and HUD-1/A forms have numerous changes. The way the forms are filled out would also have numerous changes with significant operational and technology impacts. HUD has proposed a “Closing Script” that must be read by the settlement agent at each closing. The intended purpose of the Closing Script is to ensure that borrowers understand key loan terms and features. The settlement agent must give a copy of the Script to the borrower and must read the Script out loud to the borrower. The Script compares the loan terms and settlement charges estimated on the GFE to the actual terms on the HUD-1. It explains whether those charges are within tolerances (discussed in GFE section). It describes the loan terms; and pulls information from the note, TILA, and other documents.

HUD estimates that the reading of the Script will add 45 minutes to every loan closing. Moreover, the additional time and effort to prepare the closing script will be substantial. The closing script is another example of HUD not clearly recognizing all the different nuances and processes that can occur for closings. It assumes the additional time and expense to the customer from reading the script to be minimal. Doubling the time of each closing is not a trivial consideration. HUD does not give an adequate reason why the system should be burdened with the cost.

The closing agent is supposed to be a neutral party, so the responsibility of explaining loan terms and discussing tolerances will put settlement agents in awkward position. Settlement agents will be required to answer questions about discrepancies between the HUD-1 and the GFE. However, this function is prohibited in many states, unless
performed by an attorney, leaving settlement agents open for accusations of unauthorized practice of law.

A glaring omission from the closing script instructions is what is supposed to happen when a lender fee is larger than as previously disclosed, a third party fee exceeds 10%, a customer has a question, or a customer challenges a fee. How does the closing agent know whether the “hold” period for fees expired? How does the closing agent know whether there was ever a rate lock, and if so, when it occurred? If a fee is out of tolerance does everything stop and everyone goes home without closing? Does the closing proceed if the customer still wants the loan? Who is liable if the closing is stopped but it shouldn’t have been and the buyer loses the rate lock or the house it expected to buy? Who is liable if it goes forward, but should have been stopped? If it proceeds, does that lock in a lender violation or does it constitute accord and satisfaction? If the closing agent doesn’t know the answer to the customer’s question, what happens? Is the lender at risk if it doesn’t have a representative at every closing? What if the closing agent answers incorrectly?

The script may also be a problem in states that use an escrow closing process, as a preliminary settlement statement is often not finalized when the borrower is executing the loan documents.

Many lenders have mail-away programs whereby the completed loan documents are mailed to the customer who executes them in front of a notary and returns them to the lender for recording and funding. The proposed closing script makes no provision for this highly efficient and popular loan closing method. The proposed closing script does not deal with a completely electronic application, processing, and closing, which the entire industry is anticipating will become reality within the foreseeable future for some portion of the market.

D. Mortgage Servicing Transfers – Section 3500.21

AFSA appreciates HUD’s simplification of the Servicing Disclosure Statement contents and the elimination of the mandatory acknowledgement section. The delivery requirements should be streamlined as well to simply require delivery of the Statement with the initial GFE issued in connection with an application.

E. Severability – Section 3500.22

AFSA recommends that HUD remove this provision as it could lead to inconsistent requirements.

F. The Proposed GFE Form

For the reasons set forth previously, AFSA believes that the proposed GFE application is not only unnecessary, but will create confusion for the consumer. The following comments deal with the specific sections of the proposed GFE application.
**Instructions:** These should state that the estimate is for the loan that the applicant *has applied for*, not for the terms that were approved.

**Important Dates:** The presentation of important dates is confusing and goes beyond HUD’s authority. There is no requirement regarding timing of underwriting in RESPA. Additionally, since the GFE is not a loan application, the borrower has not actually applied for a loan, and so there is not a rate offer that can be locked. The GFE should not function as a lock-in agreement. Again, it is important to note that a lot of lenders do not lock. The form does not provide for that fact.

**Summary of Your Loan Terms:** Use of the format “Your … is” in the loan details implies that these terms are approved and final, rather than the terms applied for. This has the potential to create significant confusion. Additionally, including mortgage insurance in the monthly payment without disclosing whether or not mortgage insurance is required will create confusion because mortgage insurance is not included in the note terms. Furthermore, rate lock information does not belong in this section.

**Understanding Your Estimated Settlement Charges:** In this section and in the comparison chart on page four, all types of settlement charges are combined, even those that the borrower is later told to ignore for comparison purposes. RESPA expressly allows disclosure of fee ranges; however, the proposed GFE application prohibits such disclosures. This is a direct conflict with the RESPA.

**Section-by-section analysis of the part of the GFE application entitled “Understanding Your Estimated Settlement Charges.”**

**BLOCK 1**

Limiting loan originators to a single service charge does not take into consideration state law restrictions and requirements regarding broker and lender charges. Many state usury and credit licensing laws dictate very specifically what fees are and are not allowed, and often place limits on these fees (see Appendix II). Unless HUD is able to preempt these state law restrictions, then the requirement that all originator charges be lumped into one fee, and that broker and lender fees be combined, will:

- Deprive originators of the ability to charge fees that are legally permitted under applicable state law;
- Cause the appearance of a violation of state law by originators, since they would be forced to lump separately authorized state fees into a single “service charge”;
- Impair state regulators’ ability to evaluate compliance with state law.

Block one combines broker and lender charges in one originator “service charge.” This ignores the fact that the broker and lender are separate entities, with different origination roles, and separate charges. At the most basic level, the borrower should understand who is charging what fees. When it comes to closing, the closing agent must be able to make
appropriate disbursements and balance the settlement. The proposed approach does not allow any party to the transaction to identify what amount is to be paid to the broker and what amount is to be paid to the lender. Of course it is simpler to combine the fee information and ignore the facts of the transaction, but doing so impairs, rather than improves, transparency and a borrower’s ability to shop and make an informed decision about all aspects of the mortgage transaction.

Combining the lender and broker service charge into a single charge could have the unintended effect of depriving wholesale lenders of pricing options and possibly increasing borrower's loan costs. In a brokered loan, the broker will most likely have to establish the service charge before identifying a lender. Since the service charge is not subject to change based on lender fees, any lender service charge will have to come out of total service charge quoted by the mortgage broker. As a result, brokers will naturally tend to move borrowers to lenders that cover their own origination costs by reducing the borrower credit rather than imposing a separate origination charge. For example, the broker quotes an origination service charge of $4000; the lender needs $1000 to cover the lender’s origination costs; and market pricing for an 8% loan would yield a $2000 credit. Lender A charges a service charge of $1000 and gives a $2000 credit; Lender B charges no service charge and gives a $1000 credit. Most likely, the broker will send the borrower to Lender B in order to maximize the broker's service charge, which will also have the effect of increasing the net service charge paid by the borrower. Soon all lenders will be required to price in the same manner as Lender B. The net result will be that lenders are deprived of the ability to establish their own fee structures.

If no distinction is to be made between lender and broker charges on the GFE application and HUD-1, if it is not important to the consumer how the origination service charge is divided between the mortgage broker and the lender, then that allocation should be exempted from the definition of a referral fee under 3500.14.

**BLOCK 2**

AFSA understands that option 1 was added to eliminate consumer confusion when neither of the other two options was selected. However, the statement that the credit or charge for the interest rate is included in the service charge is not an accurate description and could create confusion. This should state simply that it is neither a charge nor a credit for this interest rate.

The reference to interest rate “you have chosen” is misleading, because the interest rate may simply be a sample for disclosure purposes. The reference to “upfront charges,” is new terminology and could be confusing.

The reference to the table on page 3 should be to see “whether,” not “how,” the charge or credit can be changed, because not all lenders provide rate/point continuum options. Some lenders have set points and base the rate on the borrower’s credit rating, without the option to adjust.
The proposed definition of credit or charge for specific interest rate as relates to mortgage brokers does not accurately reflect how yield spread premiums are calculated. A lender does not pay a mortgage broker through a lump sum payment for the “loan,” because the mortgage broker does not “make” the loan and does not have a loan to sell. Instead, the YSP is calculated as a percentage of the loan amount. Moreover, the Proposal renders the concept of YSP as a lender payment to the broker obsolete. Under the Proposal, the interest rate credit or charge will be paid to/by the borrower for all loans, regardless of whether there is a broker involved. There is no longer any payment from the lender to the broker.

**BLOCK 3**

These charges, which, as identified by HUD on the sample HUD-1, generally would include appraisal, credit report, tax service, and flood certification fees, should be required to be disclosed only if the lender separately charges for these items. There is no value to the borrower to disclose a Paid Outside of Closing (“POC”) charge for these items, because the borrower has no option to shop for them. Requiring these fees to be disclosed as POC when the lender does not pass the cost on to the borrower places creates an unnecessary recordkeeping burden on the lender. If the lender does not separately charge for these fees, then they truly are lender’s overhead.

For the same reasons, the 3500.15(b)(2) affiliated business arrangement exception from the required use prohibition should be extended to include tax service and flood certification providers.

**BLOCK 4**

Title services and lender’s title insurance should be separated. Lender’s and owner’s title insurance estimates should be placed together because they have the same provider and are related. This block does not indicate whether the borrower can shop for these services.

For this and all other blocks for which the borrower is allowed to shop and select their own provider, the originator should not be required to provide a list of providers when the borrower chooses to shop. If the borrower chooses to go with the lender estimate, then the lender will select the provider, and the lender should not be required to pre-identify the provider. If not, then the borrower should research and select his/her own provider. Requiring originators to suggest alternative providers will unnecessarily expose originators to referral and steering claims.

**BLOCK 5**

It should be made clear that originators are under no obligation to offer a lender-selected provider when the borrower is allowed to shop. This block should have a place for the lender to indicate whether or not a lender-selected provider is an option. If so, then the estimate should be for the lender-selected provider’s services, and the lender should not
be required to pre-identify the provider. If not, then the estimate should be for “the cost” of these services, not for “providing” these services.

**BLOCK 6**

See remarks regarding government recording and transfer charges under comment to 3500.7(e)

**BLOCK 7**

Page 4 specifically instructs the borrower not to use estimates of taxes and insurance for comparison purposes, but the estimated escrow for these times is included in all totals that the borrower is instructed to use for comparison purposes.

Under the proposed process, an originator will not have sufficient information to develop escrow estimates. At the time of application, information about hazard insurance and tax amounts and due dates generally are obtained from the customer; however, originators are not allowed to require this additional information on a GFE application.

The current sample form of the GFE in Exhibit C, provides with respect to escrow reserve estimates that:

> As an alternative to using aggregate accounting with no more than a two-month cushion, the estimate may be obtained by using single-item accounting with no more than a one-month cushion.

This allows lenders to perform an abbreviated escrow calculation for GFE application purposes, and the limitation to one-month cushion rather than two approximates the aggregate analysis reduction. For the purposes of a GFE application, this provides a reasonable estimate of the escrows that will be required at closing. This allowance is unfortunately not included in the new GFE application instructions.

**BLOCK 8**

The daily interest charges are included in the settlement cost totals even though they are interest-rate dependent and subject to change if the interest rate is not locked. The daily interest charges will vary based on the number of days between closing and the first payment day, and under some circumstances may even be a credit. The selection of the number of days on which to base the estimate is arbitrary.

**BLOCK 9**

On refinance loans, whether or not the borrower will be required to pay the hazard insurance premium at closing depends upon the remaining policy period. Originators will not have sufficient information to determine this at the time of a GFE application.
Totals combine all fees, regardless of tolerance levels, lender control, and interest-rate dependency. While this results in one simple, easily compared amount, the end result does not provide a borrower with the information to make a meaningful comparison of settlement costs between lenders.

**Important Information and Instructions**

It should be noted that it seems unlikely that most consumers shop for their loans based on closing costs. It seems more likely that consumers shop for loans based on interest rates or monthly payments.

(Below is a section-by-section analysis of the part of the GFE application entitled “Important Information and Instructions.”)

*Shopping for a Loan Offer:* There should be some instruction to the borrower that differences in the proposed loan type, loan amount, and interest rate will affect the estimated settlement costs, that the borrower should consider differences in these factors when comparing loan offers, and that the best comparison of costs can be made when these items are the same on each estimate.

*Understanding Which Charges Can Change at Settlement:* The categories in this section do not correspond in any meaningful way to the manner in which the charges are presented on Page 2. The failure to group the fees similarly on Page 2 and in the Shopping Chart on Page 4 significantly limits the utility of using the GFE application for shopping purposes. There are too many variables in the total settlement charges for an applicant to account for without additional guidance from the form.

*Looking at Trade-Offs*

There should be a clear indication at the beginning of this section as to whether or not the originator offers trade-offs.

If the GFE application is presented with a floating interest rate, there should be no need for an originator to provide a new GFE application if the borrower expresses interest in a different rate/point combination. The borrower’s preference will be known, and the borrower and originator can discuss this further when the borrower locks the interest rate.

*Your Financial Responsibilities as a Homeowner*

The originator will not have sufficient information to provide these estimates at the time of the GFE application.
There is no tie-back to whether or not the lender will escrow for these items, so it may not be clear to the applicant whether these are included or in addition to the settlement cost estimates.

*Applying for This Loan:* This part should be deleted because there should not be two separate applications. The GFE should not be treated as a loan application.

*Shopping Chart:* Again, the Total Estimated Settlement Charges combines all fees, regardless of tolerance levels, lender control, and interest-rate dependency. As in the section, “Understanding Your Estimated Settlement Charges,” under block 10, while this results in one simple, easily compared amount, the end result does not provide a borrower with the information to make a meaningful comparison of settlement costs between lenders.

**IV. The Proposal Does Not Simplify; It Makes the Process Longer, More Complicated, Confusing and Expensive.**

In the interest of simplification, HUD proposes to quadruple the length of the GFE and a closing script to the HUD-1 closing process that requires twenty-one pages of explanation to the closing agent. Also, HUD has invented several new mathematical constructs previously unseen in the world of consumer credit.

The Proposal’s GFE lock-down concept assumes, and requires, a two step approach to applying for a mortgage that simply doesn't match many (if any) mortgage transactions out in the marketplace today. Normal mortgage transactions flow smoothly from general conversations to an application, with the GFE not slowing down the work the lender must do to determine whether it can meet the customer's need. The Proposal forces the lender to put itself at financial risk while delaying the point when it can start to do its job.

HUD's quasi-commitment concept does not work with outbound marketing. Consumers reached in this manner are not already shopping for a loan, but those who are interested have a specific financial need they want to address. The ultimate loan closed will only occasionally be identical to what might be first discussed, as (1) the actual payoffs are refined over time as better information comes in on the amount of third party debt to be paid off, (2) the value of the property when the appraisal comes in, which affects the amount of loan permitted under LTV rules, (3) the pricing changes if the valuation changes the LTV band to a different priced band, (4) re-qualification at the new price resulting from changes in the above factors, or if the customer decides to add or delete a prepayment penalty or switch from fixed rate to an ARM or vice-versa, (5) changes in the third party closing costs, as well as the exploration of different loan features that affect interest rate and monthly payment amount, such as ARM vs. fixed, prepayment penalty vs. no penalty.

One of the huge misconceptions that runs through the entire proposal is the misguided idea that, from the initial conversation there is "a loan" on which the minds have met, subject only to verification of data and the consumer's decision to proceed. Repeatedly
throughout the Proposal it states that the GFE summarizes the key terms of "the loan." This is simply an untrue assumption about the reality of where the parties are during the early phase of the loan origination process, especially when dealing with debt consolidation in the subprime space. There is no “loan.” There is no “deal.” The parties are at the outset of a process that today is designed to determine whether and what kind of loan might work.

HUD seems to have extraordinarily myopic vision about the diversity of products and practices in the mortgage market, even within the same lender. For example, in all risk-based lending multiple changes to “the deal” are normal and occur as the application moves through the process and better information comes in about all the factors that influence approval and pricing. It would not be unusual to have to re-start the whole process three or four or more times under the HUD Proposal.

V. Unintended Consequences

One possible lender response to the Proposal might be to stop offering rate locks to any applicant at least until the appraisal is in and underwriting is completed, in order to avoid being trapped into “interest dependent disclosures” set before the lender has any useful verified information for pricing the loan. This would deprive borrowers of any certainty over the interest rate, and the affordability of their payments, possibly right up to the closing date, which is hardly an improvement in the process from the borrower’s point of view. Another force that may lead lenders to cease giving rate locks would be the likely significant increase in hedging cost.

Another possible result is that some lenders would simply always quote the maximum possible third party settlement fees, rate, and lender fees, rendering the GFE of much less value to the customer.

Finally, we see massive changes in the loan closing industry resulting from the Proposal. It is too early to predict with any confidence what those changes will ultimately be, but the increased expense and risk will tend to favor larger or more efficient shops that can not only adapt to those demands, but live with the business fallout that may come from passing the costs of those changes along to the consumer. Those who do not, or cannot pass those costs along may be less viable economically in the long run. Closing agents may try to extract indemnifications from lenders, and vice versa, for disputes arising out of closings and the handling of the closing script. Again, larger organizations are more likely to have negotiating leverage to shift the risks to others. Smaller organizations may face demands to not only provide indemnifications, but some form of collateral, perhaps a bond or letter of credit, due to lack of their financial strength, all of which will put them at a financial disadvantage.
VI. Reform for Pricing of Services Will be Ineffective

A. Average Cost Pricing

The Proposal allows lenders and brokers to use average cost pricing for settlement services within any class of transactions. The rule currently has two options for determining the average price: (1) actual average price for the service on all loans closed by the loan originator in a geographic area over the averaging period; or (2) the average price based on a tiered price contract for the service if the projected number of loans used in the calculation is equal to the actual number of loans actually closed during the averaging period. These averages must be calculated based on a recent period of six consecutive months. HUD’s authority to allow this under current law is questionable. This section only applies to settlement services provided by third parties, not lenders or broker services. “Class of transactions” is not defined and would need to be defined to determine if the methodology used to define the class is allowed, such as: loan types, geographic regions, etc.

The method for determining average cost must be constantly updated by the class of transactions with the duty on the loan originators to retain all supporting documentation, but burden on actual settlement service providers to demonstrate compliance with requirements.

Average cost pricing would be shown on the GFE and HUD-1 as the price charged to the consumer, but the actual amount paid to the provider would be the contractual fee, which could be greater or less than the average cost. The Proposal should advise the settlement agent on how to handle the difference.

B. Negotiated Discounts

The rule proposes to amend the currently defined “thing of value” to exclude negotiated discounts charged to borrowers by settlement service providers from the definition. Since Section 8 of RESPA prohibits the giving or receiving of a "thing of value" in return for the referral of business, the deletion of negotiated discounts from the definition would allow the negotiation of a discount from service providers without violation of RESPA. All discounts negotiated must be passed through to the borrower. Discounts can only be negotiated by a settlement service provider, which arguably does not include builders. The builders could not negotiate a discount that included the house price as part of the purchase transaction. Since all discounts must be passed on to the borrower, if the borrower does not pay for the settlement service, then it would not appear to fit within this exception, such as a "no cost" loan.

C. Markups of Third Party Fees

The proposed change to section 3500.8 of Regulation X appears to prohibit the mark-up by a lender of any third-party fee. This change conflicts with current HUD guidance,
which permits mark-up if the lender provides additional services and the amount of the
mark-up is reasonably related to the additional services.

VIII. Conclusion

In attempting to develop a comprehensive solution to RESPA reform, HUD has run into
the hurdles that have affected several of its previous attempts: the restrictions of a narrow
legislative mandate, the jurisdictional jigsaw puzzle of consumer credit regulations
divided across several agencies, a lack of collaboration amongst the agencies in
developing a coordinated system for issuing regulations jointly, and finally, the incredible
complexity and diversity of the residential mortgage market in the U.S. This makes it
extremely challenging to fashion rules that effect needed change, are practical, and don’t
harbor major unintended consequences.

One model HUD might consider for increasing the odds of a successful reform effort
would be to work with the other agencies charged with portions of the residential
mortgage credit governance to create a standing body, perhaps like the FFIEC, to develop
mutually consistent regulations, commentary, and guidance on parallel paths.

Such collaboration would also provide the benefit of facilitating development and
submission of integrated proposals to Congress for statutory authorization needed to
support comprehensive regulatory reform.

AFSA appreciates the opportunity to comment on the Proposal. Please feel free to contact
me with any questions at 202-296-5544, ext. 616 or bhimpler@afsamail.org.

Respectfully submitted,

Bill Himpler
Executive Vice President, Federal Government Affairs
American Financial Services Association
APPENDIX I - Answers to Specific Questions

1. Whether a 12-month implementation period for the Good Faith Estimate ("GFE") is appropriate.

A 12-month implementation period for the GFE will not be sufficient. Currently, lenders are expending considerable resources to comply with the expected amendments to TILA, as proposed by the Board. AFSA respectfully requests that HUD allow for a 24-month implementation period.

2. The proposed GFE, as well as the proposed HUD–1/1A Settlement Statement Forms.

AFSA’s comments on the proposed GFE and the proposed HUD-1/1A Settlement Statement forms are above.

3. Possible additional ways to increase consumer understanding of adjustable rate mortgages.

AFSA appreciates HUD’s efforts to try to increase consumer understanding of adjustable rate mortgages. However, AFSA believes that Congress has delegated that responsibility to the Board. Currently, the Board is working to increase consumer understanding of adjustable rate mortgages through its amendments to TILA.

4. Whether the proposed requirements for completing and delivering the Addendum to the HUD–1/1A, including the mandatory reading of the Closing Script by the party conducting the closing to the borrower(s), are the best methods for assuring that borrower(s) understand their loan terms and the differences between the GFE and the HUD–1/1A.

Here again, AFSA appreciates HUD’s efforts to try to ensure that borrowers understand their loan terms. However, that responsibility rests with the Board, which is currently reviewing mortgage disclosures to make sure that borrowers understand their loan terms.

Additionally, AFSA notes that not all closings are done in person. AFSA is requesting that HUD allow the closing script to be given over the phone.

AFSA also asks that HUD provide a safe harbor to lenders in the person reading the closing script makes an inadvertent error. This could open lenders up to litigation.

5. Whether a provision should be added to the RESPA regulations allowing 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 should such a provision be structured? (Section IV.E. 10) Would such a provision be useful, and if so, what would be the appropriate time frame for finding and refunding excess charges? Could such a provision be abused, and therefore harmful to consumers?
Would the ability of prosecutors to exercise enforcement discretion obviate the need for such a provision?

HUD does not have the authority to enact such a provision. Congress would have to amend RESPA to give HUD the authority to enact this type of provision.

However, if such a provision were enacted, AFSA requests that HUD add a right to cure to the proposed regulation. Lenders should be able to send the correction within sixty calendar days of the discovery of the error.

6. Proposed methods for calculating average cost prices and on any alternative methods that should be permitted. (Section IV.H.) Specifically, how to define ‘‘class of transactions.’’ Comments are also invited on alternative average cost pricing methods and other pricing methods that benefit consumers and are based on factors that would lead to charges to the consumer and disclosure of such charges that are easily calculated, verified, and enforced, but difficult to manipulate in an abusive manner. Such factors could include:

   a. Experience over a period of time that is longer or shorter than that currently provided in the proposed rule;
   b. Prices for the service among the usual third party providers upon which the lender or other settlement service usually relies;
   c. General industry practices; and
   d. A reasonable projection of future costs.

AFSA does not have a comment on this question.

7. Whether the proposed change in the definition of ‘‘required use’’ will better serve the purposes of RESPA and whether further improvements could be made in the definition to accomplish the intent of both the affiliated business exemption in section 8 and the prohibition in section 9 on the required use of a title company.

While HUD has attempted to clarify the definition of “required use,” it seems as though HUD, perhaps inadvertently, has created a presumption of a violation.

8. With respect to the revised definition of “Good Faith Estimate” set forth in the proposed rule language at 24 CFR 3500.2, is the standard set forth sufficient to ensure that good faith estimates will be filled out consistently by all loan originators in a particular community?

AFSA believes that the definition of “Good Faith Estimate” is unclear. It is no longer a “GFE.” AFSA asks that HUD clarify how this definition is different from the current definition.

9. Should the Section 6 disclosure on transfer of servicing that is required under RESPA be included on the GFE?
The Section 6 disclosure should not be included on the GFE.

10. Should a loan originator be required to include a “no cost loan” on the trade-off chart on page 3 of the GFE as one of the alternative loans if it is not the loan for which the GFE is written?

AFSA asks that HUD explain what is meant by the term “no cost loan.” Also, if a lender does not offer a “no cost loan,” should the lender still have to include it on the trade-off chart? Many lenders do not offer “no cost loans.”

11. HUD recognizes that there may be incidental or nominal costs to provide GFEs to prospective borrowers. Therefore, in order to facilitate shopping using GFEs, the proposed rule would allow a loan originator, at its option, to collect a fee limited to the cost of providing the GFE, including the cost of an initial credit report, as a condition for providing a GFE to a prospective borrower. HUD is interested in receiving comments on this approach.

AFSA agrees that it is necessary for lenders to be able to collect a fee to recoup the cost of providing the GFE. However, this is at odds with certain state laws.

AFSA would like HUD to work with the Board to clarify whether the fee would be included in the APR.

12. HUD welcomes comment on these and any other pricing techniques that may result in greater competition and lower costs to consumer and that are consistent with the purposes of RESPA.

AFSA does not have a comment on this question.
APPENDIX II – State Law Restrictions and Requirements Regarding Broker and Lender Charges

The requirement that all charges to be paid by the borrower that are to be received by all originators for, or as a result of the loan origination be disclosed as a single service charge, see 73 Fed. Reg. at 14047, 14049, fails to take into consideration state law restrictions and requirements regarding broker and lender charges. Many states have complex regulatory schemes governing allowable fees, fee amount and timing limitations, treatment of fees as interest or finance charges, refundability, disclosure requirements, and other related requirements and prohibitions. As examples:

♦ A California Residential Mortgage Lender Licensee is allowed to collect prior to closing an application fee, a lock-in fee provided there is a written lock-in agreement meeting statutory requirements, and a commitment fee provided the written commitment meets statutory requirements. Cal. Fin. Code § 50203.

♦ The Idaho Residential Mortgage Practices Act allows a licensee to collect an application fee, a rate-lock fee, and a commitment fee prior to closing. Idaho Code § 26-3113(1).

♦ The Mississippi Mortgage Consumer Protection Law limits lenders to compensation not exceeding 7.95% of the original principal balance; however, a lock-in fee collected in accordance with statutory requirements is excluded from this amount. Mississippi Code §§ 81-18-27(1)(j), 81-18-28.

♦ New York Banking Board Regulations allow mortgage brokers and mortgage lenders to collect separate application fees and processing fees. N.Y. Comp. Codes R. & Regs. tit. 3, § 38.3; N.Y. Comp. Codes R. & Regs. tit. 3, § 80.8

♦ The Tennessee Department of Financial Institution’s Rules Pertaining To Mortgage Lending, Loan Servicing And Loan Brokering permit lock-in and commitment fees and expressly define these fees as not including interest. Tennessee Rules § 0180-17-.01(5), (7).

♦ The Texas Finance Code allows a mortgage broker to charge a number of fees prior to closing, including fees for processing a mortgage application, for taking a mortgage application, for automated underwriting, for a courier service, to issue a loan commitment, or, subject to certain requirements, for locking in an interest rate. V.T.C.A., Finance Code § 156.304(a); Tex. Admin. Code tit. 7, § 80.8

The proposed prohibition against separately itemizing originator charges for “origination services” has a substantive impact that is not contemplated by RESPA, and HUD does not have preemption authority to eliminate the genuine tension between federal and state law that this requirement will create. As a result:
♦ Originators will be deprived of the ability to charge fees that are legally permitted under applicable state law;

♦ RESPA disclosures may appear to indicate state law violations, leading originators to develop secondary disclosures providing originator service charge breakdowns, further complicating the loan origination process; and

♦ State regulators’ ability to evaluate compliance with state law will be impaired.