Financial Services Regulatory Practice

Regulatory Practice Letter

ADVISORY

RPL Number 09-07

Department of Housing and Urban Department (HUD) – Final Rule on Real Estate Settlement Procedures Act (RESPA)

Executive Summary

On November 12, 2008, the U.S. Department of Housing and Urban Development ("HUD") issued its final rule on the *Real Estate Settlement Procedures Act* ("RESPA"). The final rule includes provisions standardizing the Good Faith Estimate ("GFE") form; ensuring clear summary of loan terms and total settlement charges; providing more accurate estimates of closing costs; improving disclosure of yield spread premiums; facilitating comparison of the GFE and HUD-1 Settlement Statement; clarifying HUD-1 instructions; and strengthening the prohibition of required use of affiliated businesses. Some of the new provisions were required to be implemented on January 16, 2009. The effective date of the revised definition of "required use," which would have become effective January 16, has been delayed until April 16, 2009 because of recently initiated litigation. Other provisions, including the use of new GFE and HUD-1 forms, will become effective January 1, 2010.

Background

RESPA is a consumer protection statute that was first passed in 1974 and is enforced by HUD. It applies to mortgage transactions secured by loans on one-to-four family residential properties, and is intended to help consumers become better shoppers for settlement services, as well as to prohibit certain practices that unnecessarily increase settlement costs. Under RESPA, lenders are required to disclose loan terms and settlement costs to consumers at various times in the transaction using the GFE and HUD-1 forms.

In 2002, HUD proposed rules to simplify and standardize the disclosure process under RESPA. More than 40,000 comment letters were submitted in response to this proposal though the only consensus among the comments was the need for reform. The proposal was subsequently withdrawn in 2004, and HUD pursued a series of public and interagency efforts to better inform future RESPA revisions. On March 14, 2008, HUD again proposed changes to

Subject:
Final Rule on RESPA to Simplify and Improve the Process of Obtaining Mortgages and Reduce Consumer Settlement Costs

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RESPA intended to make the mortgage process clearer and less costly for consumers. Approximately 12,000 comments letters were received on this proposal. Notable among the letters was a consensus from members of Congress and the industry that HUD should wait to finalize its proposal in order to better coordinate with the Federal Reserve Board ("Fed") on the Fed's efforts to reform mortgage loan disclosures under its Regulation Z, which implements the *Truth-in-Lending Act*.

HUD published its final rule on RESPA on November 17, 2008. In its final form, the rule is substantially the same as proposed with some modifications based on public comment, including, but not limited to:

- A shorter revised GFE form;
- Elimination of a "closing script" to be completed and read by the closing agent; and
- Adoption of requirements for the GFE form that are similar to the Fed's revised Regulation Z with regard to fees charged in connection with early disclosures and defining timely provision of disclosures.

Description

Some key changes that the final rule made to RESPA include:

1. Standardizing the GFE Form

Lenders are required to provide consumers with the new GFE form within 3 days upon the receipt of an application. This 3-page GFE form includes standardized tables and charts. For instance, it requires summaries of loan terms and monthly escrow obligations on the first page, estimates of settlement charges in pre-fixed categories on the second page, and comparison charts on the last page.

The final rule also requires lenders to make the estimates for all non-interest rate related settlement charges and loan terms available for at least 10 business days after the GFE is provided, allowing borrowers to have time to shop among other lenders.

2. Ensuring more accurate estimate of closing costs

HUD imposes 3 separate categories of settlement charge estimate tolerance:

(1) *Zero tolerance* – lender's own origination charges and underwriting fees, yield spread premiums/discount points, adjusted origination charges, and transfer tax charges;
(2) *10% tolerance* – required services by a third party provider selected by lender, title services and lender's title insurance selected by lender, and government recording charges;
(3) *Non-restricted tolerance* – service fees by third party provider selected by borrower, initial escrow deposit, daily interest charges, and homeowner's insurance cost.

HUD also permits the use of average calculation for service charges, but lenders are still accountable for the tolerance limitations.

3. Improving disclosure of yield spread premiums

Under the final rule, HUD has provided additional instructions to lenders on how to disclose lender' credits or charges. Lenders need to disclose all internal origination fees as lender's origination charges and premiums as "a credit of $___ for this interest rate of ___%". Any lender payment is then subtracted and any points are added to come up with the "adjusted origination charges."

4. Facilitating GFE and HUD-1 comparison

The new HUD-1 form contains a fee comparison table that lists the estimated fees identified on GFE and actual fees charged at closing side-by-side, allowing direct and line-by-line comparison.

5. Strengthening the prohibition of required use of affiliated businesses

The final rule modifies the current definition of "required use" so that consumers are more likely to avoid potentially deceptive referral arrangements. The new definition identifies economic disincentives for improperly influencing consumer's choices and defines untrue referral incentives as problematic. The new definition also extends the rule to "persons" rather than only "borrowers". Accordingly both the buyers and sellers of the property are eligible to receive discounts under the final definition.

The required use rule does not apply to service providers who can offer "a combination of bona fide settlement services at a total price" lower than the sum of the market prices of the individual settlement services.

6. Implementing other technical amendments

The final rule modifies the language used in the transfer of servicing disclosure form, eliminates the phase-in period for aggregate accounting of escrow accounts, and clarifies the applicability of electronic signatures.

Effective Dates

- *January 16, 2009* – (1) changes on servicing disclosure statement, (2) use of average cost pricing, and (3) the technical changes;
- *April 16, 2009* – use of new definition of required use; and
- *January 1, 2010* – (1) use of new GFE and HUD-1 forms (including yield spread premiums disclosure and tolerance restrictions), and (2) all other definition and requirement changes.

The new GFE form may be used prior to the effective date, as long as all new GFE requirements, including compliance with the tolerance restrictions and the use of the new HUD-1/1-A, are followed.

Grace period

Lenders and settlement service providers have 30 days after settlement to correct potential disclosure or tolerance restriction violations.

KPMG Commentary

In comment letters and Congressional testimony, lenders have expressed their concerns about the potentially staggering cost and time needed to implement the new RESPA requirements. Given the number of changes required by the final rule, high compliance costs are expected for items such as altering systems and software, seeking compliance and legal consultation, ensuring compliance and audit testing and providing training to staff, etc.

Institutions are encouraged to start their planning and implementation process early to ensure that all rules will be complied with on time and process/system changes are integrated accordingly.

In the preamble to the final rule, HUD expressed its willingness to work further with the Fed to better coordinate disclosures under RESPA and TILA. However, HUD states it felt compelled to finalize the rules at this time in order to ensure better settlement disclosures for consumers now given the trouble within the mortgage industry and the understanding that a significant number of consumers do not understand the disclosures currently provided to them.

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