

**STATEMENT OF
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GALENA, ILLINOIS,
CHAIR, GOVERNMENT AFFAIRS COMMITTEE**

**ON BEHALF OF
THE AMERICAN LAND TITLE ASSOCIATION**

**BEFORE THE
COMMITTEE ON SMALL BUSINESS
US HOUSE OF REPRESENTATIVES**

**RESPA REFORM
AND THE
ECONOMIC EFFECTS ON SMALL BUSINESS**

MARCH 11, 2003

Mr. Chairman, my name is Gregory M. Kosin, and I am the President of H.B. Wilkinson Title Company, Inc., in Galena, Illinois. I am also the Chairman of the Government Affairs Committee of the American Land Title Association,¹ and serve as an Abstractor and Title Agent Representative on ALTA's Board of Governors. I appreciate the opportunity to appear today at this very important hearing on behalf of the ALTA, which represents over 1,750 title insurance agents, most of which are small businesses. Accompanying me is Ann vom Eigen, ALTA's Legislative and Regulatory Counsel.

The title and settlement services industry has traditionally been an industry in which there have been few barriers to entry by small businesses and in which small businesses have thrived. This is due in part to the local nature of our business – serving the needs of customers in local real estate transactions – and to the fact that we are also a highly service-oriented business where meeting the needs of local customers has been an important factor, in addition to having competitive fees.

We believe that the HUD proposed revisions to the RESPA regulations, particularly the Guaranteed Mortgage Packaging proposal, would have a very serious adverse effect on small businesses in our industry, and on our ability to compete for consumer business. Equally important, we believe that the proposals, if implemented in their present form, would effectively close the door to future entry into this business by small businesses.

It is clear that HUD is aware of these consequences, but believes that the adverse impact on small business is outweighed by (a) the likelihood that major lenders will be able to

¹ The American Land Title Association membership is composed of 2,300 title insurance companies, their agents, independent abstractors and attorneys who search, examine, and insure land titles to protect owners and mortgage lenders against losses from defects in titles. Many of these companies also provide additional real estate information services, such as tax search, flood certification, tax filing, and credit reporting services. These firms and individuals employ nearly 100,000 individuals and operate in every county in the country.

obtain deep discounts from settlement service companies who will want to be part of their packages, and (b) the prospect that mortgage lenders will pass through to their borrowers the benefits of such discounts. HUD estimates that small businesses will lose somewhere between \$3.5 billion and \$5.9 billion in annual revenues if their proposals are implemented. Whether these estimates are accurate – or too low – is not the critical issue. The critical issues that we hope this Committee will focus on are:

- why is HUD so willing to tilt the playing field in favor of large lenders; and
- why is HUD so cavalier about the adverse impact on small businesses, which have been a mainstay of this industry, an industry that has provided opportunities for employees of larger companies to strike out on their own and develop their own businesses.

Why do we believe that the HUD proposals will undermine the role of small business in the title and settlement services industry?

First, because of the incentives HUD has provided for packaging, it is clear that the market will move substantially in that direction, rather than towards the revised good faith estimate (GFE) regime.

Second, while HUD maintains that “anyone can provide packages” under its proposed Guaranteed Mortgage Package regime, because the GMP Agreement offered to consumers must include a loan at a guaranteed interest rate it is highly unlikely that anyone other than lenders will be in a position to effectively offer GMPAs. The mortgage lending industry has become increasingly concentrated. In the last 5 years the top 10 mortgage originators have doubled their market share from 25% to 50%.² The HUD packaging proposal will also have the effect of increasing the concentration in the title and settlement services industry.

Third, by granting a broad exemption from RESPA § 8 for its GMPA proposal, HUD is encouraging lenders to seek, and settlement service providers to offer, discounts and other

² “Consortium Approach Gains in Home Loans,” American Banker, July 12, 2002, at 1, 10.

benefits in order for the providers to be included in the lenders' packages. In that kind of environment – where the lender rather than the consumer is going to make the choice of provider – the bigger title and settlement service companies are far better positioned to offer such discounts and inducements than the small business provider.

Fourth, if the packaging regime becomes widespread, as is likely to happen because it has the backing of the major mortgage lenders in the country, providers of title and settlement services will only be able to market their services to and through lenders. Lawyers and title companies that today are able to obtain business by direct contacts with the consumer will be faced with the situation where the lender, and only the lender, decides which attorney or which title company will be part of its package, and the consumer will have to accept that selection if it wants a loan from that lender. These adverse effects will be particularly severe in rural areas of the country where local attorneys and title companies will inevitably find that they cannot gain entry to the packages of the major lenders operating in that area.

The competitive advantage of small businesses – service to the consumer – will be undermined because the only successful marketing approaches will be those that enhance the profitability of the packages sold by the lenders. Likewise, there will be fewer competitive opportunities for new small businesses to enter this market since the only way they will be able break into the market will be to offer even greater discounts to lenders than those lenders can obtain from the major settlement service companies. This is unlikely to happen.

A review of the economic analysis on which HUD has based its evaluation of the savings associated with the changes proposed in their rule raises many questions. HUD appears to have relied heavily, in their assumptions, on an extrapolation of data from FHA loans, which represent a small portion of the mortgage market, are typically lower priced homes, not typical examples of the residential housing market. Consequently, the sample on which the analysis is based is not typical.

In essence, the HUD packaging proposal is predicated on the expectation that there will be a substantial shift of revenue from settlement services providers to the major mortgage lenders, who will have the economic clout to obtain discounts as the price of entry into their packages, and that most or all of this revenue shift will be passed on to consumers. Apart from the fact that this is an artificial shift in revenues for which there is no significant justification, it is questionable how much of these discounts and rebates will trickle down to the consumer. The fact that so many major mortgage lenders are so strongly in favor of packaging suggests that they believe the profits from packaging are likely to be significant.

HUD also estimates substantial savings to both consumers and service providers through reduced time spent in shopping for services and responding to consumer concerns. While we believe the source and estimate of these savings is very uncertain, we also question whether elimination of time spent with consumers is a worthwhile goal. Consumers deserve to make informed decisions about the financial products and the services they choose.

In this environment, the backbone of our industry – the smaller abstractors and title agencies – will not have the resources to be able to offer the kind of discounts and payments that the larger companies can provide. Based on a survey conducted by ALTA in 2002, which was a boom year for the real estate industry, 51% of the title insurance agents and abstractors in the country had less than \$500,000 in gross revenue in 2001, and 72% had less than \$1 million. 68% had 10 or fewer employees, and 42% had less than 5. These individuals and companies have demonstrated that they can effectively compete with anyone for the consumer's business, but in a world in which major lenders are able to use the clout derived from the volume of transactions they handle to extract discounts from major providers, these small businesses will simply be unable to compete on that basis.

HUD's economic analyses concludes that lower prices for originators and third party settlement service providers will drive out the less efficient firms, with the more efficient firms surviving and doing the work. This fails to recognize the current reality of the local marketplace

and its potential evolution. Many counties in this country currently have only one closing or title agent. Some of these firms may be inefficient. However, particularly in rural areas, implementation of packaging could eliminate some of those providers, and consumers may not have any access to those services. HUD has even posed questions in its proposed rule, the validity of state law. Specifically, HUD has asked what state laws merit pre-emption. Many state laws relating to title insurance, such as rate regulation, are designed as consumer protection measures which ensure adequate access to these services at a reasonable price.

Mr. Chairman, if small businesses cannot compete effectively with their larger competitors for the consumer's business, then, in the long run, they are not going to survive. But HUD's proposals do not create a playing field in which the most efficient, or the best, competitors end up winning the race. Rather, HUD's proposals create a playing field in which those lenders with the most clout, or those service providers who are best able to offer significant inducements to lenders to get into their packages, will end up winning the race. Small lenders may be very efficient at making mortgage loans, but if they lack the clout to obtain the kind of discounts that their larger lender competitors can squeeze out of service providers, they will not be able to compete effectively. In other words, they will lose market share not because they are inefficient lenders, but because they cannot command the kind of discounts from third-party providers that their larger competitors can command.

Similarly, smaller title companies or smaller providers of settlement services have demonstrated that they can compete effectively with their larger competitors in providing title and settlement services. But in the competitive world that HUD wants to create, these companies could well lose market share to their larger competitors who are in a better position to offer discounts or other things of value to lender-packagers. This would enable those lenders to realize greater profits on their packages than by including smaller providers in their packages. Again, smaller title companies and other settlement service providers will lose market share not

because they are inefficient providers of settlement services, but because they cannot provide the kind of discounts that their larger competitors can offer.

The bottom line is that consumers will effectively have fewer choices in their selection of providers of legal and title-related services for their real estate transactions. Under HUD's approach, the consumer selects the lender and must accept whatever service providers are in that lender's package. This is a problem with regard to services, such as those provided by lawyers and title companies and agencies that are provided for the benefit of the purchaser and seller of the real estate.

Consumers should have choice in the selection of their service providers, and this will not be possible under the Guaranteed Mortgage Package Agreement. In addition, HUD has estimated that some of the economic benefits of packaging will be time savings because consumers will not shop for settlement services, and lenders and settlement service providers will not have to answer questions. Achieving savings through reduced knowledge and understanding by consumers of their personal financial investments is not a good result.

The ALTA Board has agreed to explore litigation should HUD come out with a final rule similar to the proposed rule. In fact, the HUD proposal is particularly objectionable in that the Agency lacks statutory authorization to take this step. Indeed, the proposal is in conflict with the disclosure regime that Congress did adopt in RESPA. If HUD was implementing the clear will of Congress, then we would have to accept the consequences of the policy decisions reflected in the laws of the United States. But that is not what is going on in these proposed regulations. Here, HUD believes that it has come up with a better regulatory regime than the one Congress adopted and is prepared to have small business squeezed out of the lending and settlement process because it believes that the discounts and rebates obtained by the large lenders will, as a result of competition among mortgage lenders, be passed on to consumers. This is a questionable assumption at best. But, what is of overriding importance, is that it does not implement – or, indeed, even reflect – any policy judgment that has been made by Congress.

HUD should not undermine the historic role of small business in one of the key sectors of the American economy without clear legislative authorization and direction. In this regard, ALTA's outside counsel has prepared an analysis of HUD's lack of statutory authorization, which I will submit for inclusion in the record of this hearing. It is particularly ironic that, at the same time HUD is pursuing a "packaging" approach that so clearly favors large companies over smaller business entities, the Bush Administration has proposed a strategy to all federal agencies calling on them to reduce the adverse impact on small business resulting from the "bundling" of federal contracts. As discussed in the October 2002 OMB report entitled "Contract Bundling: A Strategy for Increasing Federal Contracting Opportunities for Small Business," bundling of federal contracts has been an increasing practice in recent years so that fewer, larger groupings of contracts are put out for bid. While such bundling has made things easier for federal contracting officers and their agencies, it has had the effect of eliminating competitive opportunities for small businesses which want to compete for government contracts. To counteract that trend, OMB has urged executive branch agencies to revise their regulations to eliminate unnecessary contract bundling and, in the words of the Administrator of OMB's Office of Federal Procurement Policy, to make "a significant step forward towards ensuring that small businesses and entrepreneurs have access to federal contracting opportunities." It seems to us that HUD's packaging proposal is completely out of step with the thrust of OMB's "unbundling" approach to government contracts.

We are deeply concerned that the HUD packaging proposal will unfairly and unreasonably eliminate competitive opportunities for small business. We thank you for holding this hearing to address this issue.