May/June 2008

TitleNews

Official Publication of the American Land Title Association

Deciphering RESPA

HUD's Proposed Rule and Impacts on the Title Industry

Inside This Issue:

Recognizing Mortgage Fraud, Part II

Stop Marketing! Start Re-Marketing!

Boost Productivity with Integrated Technology

Prsrt Std
U S Postage
PAID
Merrifield, VA
Permit # 6418

Deciphering RESPA

HUD'S Proposed Rule and Impacts on the Title Industry

Despite HUD's goal of simplifying the settlement process, the department has created a complicated rule that promises to be controversial. Read about the most important changes to RESPA and what they mean for the title industry.

The wait is over. On Friday, March 14, 2008, the U.S. Department of Housing and Urban Development (HUD or department) published its proposed regulations to reform the Real Estate Settlement Procedures Act (RESPA). HUD partially titles its rule a "Proposed Rule to Simplify and Improve the Process of Obtaining Mortgages"; however, the rule appears to be far from simple. >>

In addition to expected changes to the Good Faith Estimate (GFE), HUD proposes to introduce tolerances for settlement charges, require a new format for disclosure of yield spread premiums, modify the HUD-1 Settlement Statement (HUD-1), introduce a new closing script, and amend certain established RESPA definitions, to name a few. As a result, RESPA reform is never without controversy, and HUD appears to have created a complicated and controversial rule. Accordingly, this article summarizes the most important changes proposed by HUD's rule, and identifies certain practical issues that may impact the title insurance industry.

RESPA reform is never without controversy, and HUD appears to have created a complicated and controversial rule.

I. Seven Main Components of Proposed Rule

A. Good Faith Estimate

The GFE is the signature piece of the 2008 proposed RESPA rule. HUD's proposed rule takes the current one-page, suggested form for the GFE and requires a mortgage originator to provide a four-page standardized form within three days of receiving a GFE application. This proposed form would include a summary of the key terms of the loan as well as an estimate of total settlement charges. The rule would require a mortgage lender or broker to keep the GFE's offer for settlement costs open for ten business days to allow the consumer to comparison shop with other loan originators. With regard to the initial interest rate, the GFE must acknowledge that the rate is available until a specified date. Until that rate is locked, however, the initial interest rate may continue to float.

1. Tolerances
Related to the estimate of settlement charges on the GFE, HUD proposes to create three separate categories of settlement charges and subject them, absent "unforeseeable circumstances," to different tolerances. The first category of fees would be subject to a zero tolerance standard, meaning the fees estimated on the GFE may not be exceeded at closing (i.e., lender's own service charge, recording fees). HUD would subject the sum of the fees in the second category to a 10 percent tolerance. While each individual fee in this category may increase or decrease, the sum of the total increases may not exceed 10 percent at closing (i.e., appraisal fees, title insurance fees if the services are obtained from a lender-recommended provider). The final category of fees would be subject to no restriction, meaning HUD would not limit the amount of any increase in the fees. These fees, therefore, may increase by more than 10 percent at closing (i.e., daily interest, title insurance fees if the borrowers shop for their own provider).

2. Disclosure of Yield Spread Premiums
Although current RESPA regulations require yield spread premiums to be disclosed as paid to a mortgage broker outside of closing, HUD's proposed rule would require such fees to be disclosed on the second page of the new GFE form as a "credit or charge for the specific interest rate chosen." The "credit" in this case encompasses a yield spread premium, and the "charge" is meant to denote the presence of discount points.

3. GFE Fees
In modifying the GFE, HUD states its preference that mortgage lenders and mortgage brokers not impose any charges for a GFE. The department, however, acknowledges that there may be incidental or nominal costs in providing GFEs to prospective borrowers. The rule, therefore, proposes to permit a lender to charge a fee but limits the amount to a lender's actual costs, including the cost of an initial credit report.

4. FHA Origination Fees
Finally, under current FHA regulations, HUD limits the amount of an origination fee a mortgagee may collect to one percent of the loan amount. In the proposed rule, HUD has recommended that this limitation be removed. The department appears to believe that its new rule on the disclosure of settlement charges and tolerance limitations will force lenders to reduce their origination prices which, in turn, will alleviate any need for a maximum FHA origination fee.

Offer electronic closings to your customers today with Stewart's eClosingRoom.™

Are you ready to offer your buyers and sellers something more? Differentiate yourself in the market by offering your clients a service unique to your company. With Stewart's eClosingRoom you can give customers electronic closings that reduce closing times to 20 minutes, grow your market share and leave your competitors crying over their huge stacks of paper.

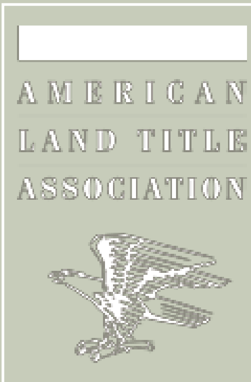
Offer electronic closings today, don't wait for tomorrow. Contact us right away to get 20-minute closings™ with Stewart's eClosingRoom.

stewart®

(866) 60-TOOLS (86657) | stewart.com/eClosingRoom | smarttechnology@stewart.com

ALTA Comments on RESPA

The following interview with CEO Kurt Pfotenhauer describes how the association is tackling this difficult and important issue.



Why did HUD come out with this rule?
HUD's goal is to simplify the mortgage loan and settlement process and make it more transparent for consumers. While we certainly agree with that goal, we feel HUD's proposal falls considerably short and only creates more confusion in a process that is already mired in regulatory procedures and requirements.

How does it fall short?
For one, it would impose a burden on settlement agents by requiring them to prepare and read a detailed "closing script" at settlement that includes an explanation of the loan terms which, in many states, is the function of an attorney. The proposal also arguably puts more control over the selection of settlement service providers into the hands of large national banks, to the detriment of local banks and local title agents/abstracters.

What is ALTA doing?
We have had staff, the Government Affairs Committee, and expert consultants pouring through the proposal to determine its impacts. We also have solicited broad member input as to how this would affect their businesses. This is a complex rule that has more than 100 pages of text and a 500-page economic analysis. The department spent four years drafting the proposal, and they've given us two months to fully explore all the ramifications from a business, economic, regulatory, and consumer perspective. We've asked for an extension, and hope that by the time this goes to print, we'll have received it.

Secondly, we have been actively talking to members of Congress to educate them about the negative impacts of the rule and to request hearings on certain aspects of the proposal. Third, we are engaged with the Small Business Administration to bring its voice into the mix on behalf of all our small, independent agents who may be adversely affected. Fourth, we are engaged in discussions with other real estate trade associations—REALTORS®, mortgage bankers, brokers, and others—in an effort to unify our approach. Finally, we are engaging HUD directly and arguing our points face-to-face.

Where can members find additional information about the new rule and the industry's position?
The actual proposal and other materials are posted on ALTA's Web site. Additional materials will be posted as soon as they become available. Meanwhile, there is a very good article in this issue of *Title News* that describes, in more detail, how the rule would impact our industry.

What are the next steps?
We will continue to work with members of Congress and other trade associations in an effort to deal with issues raised by the proposal. We also will attempt to work with HUD to help craft meaningful alternatives to some of the more onerous requirements. Finally, we are asking our members to communicate the industry's concerns to their representatives of Congress.

For more information, go to www.alta.org, Federal Issues/RESPA Reform.

B. HUD-1 Settlement Statement

1. HUD-1 Form

While the current GFE and HUD-1 do not match or allow for easy comparison, HUD proposes to alter the HUD-1 form to allow a consumer to directly compare the fees identified on the GFE to those fees charged at closing. Specifically, the Department proposes to bold certain text and include bracketed language on the HUD-1 that identifies the section of the GFE where a consumer will find the estimated charge.

In addition, while the current HUD-1 requires a lender or mortgage broker to itemize their internal origination charges, such as processing fees and document preparation fees, the modified HUD-1 would require only the lender's bundled "service charge" to be disclosed at closing. Similarly, rather than itemize fees for primary title services, such as the title search, title examination, and title binder, the modified HUD-1 provides for a single "title services and lender's title insurance" fee to be disclosed on the HUD-1. This category of fee matches that on the proposed GFE form. However, the split in title premiums between the agent and underwriter would be separately disclosed.

2. Mark Up of Third-party Fees

In addition to the changes HUD proposes to make to the HUD-1 form itself, the rule proposes to include new language in Section 3500.8 of the RESPA regulations. This language would state as follows: "The amount stated on the HUD-1 or HUD-1A for any itemized service cannot exceed the amount actually received by the third party for that itemized service, unless the charge is based on an average cost price in accordance with paragraph (b)(2) of this section." If read literally, this language seems to suggest that the markup of third-party fees would be prohibited under the new rule.

Phil Schulman holds up a sample of the Good Faith Estimate during a special session at the ALTA 2008 Federal Conference titled: "ALTA Perspective on Proposed RESPA Rule." Attendees were given a preview of ALTA's analysis of the rule and how it will affect the title industry.

C. Closing Script

The rule also proposes to create a new addendum to the HUD-1, or a closing script, which the settlement agent is tasked with preparing, reading aloud to the consumer at closing, and providing in hard-copy format to obtain the consumer's written acknowledgment. Essentially, the rule would require the settlement agent to explain specific loan terms as stated in the mortgage note, such as interest rate, monthly payment amount, and the presence of a prepayment penalty and balloon payment. The settlement agent also must compare the loan terms and settlement charges to those estimated on the GFE and indicate whether certain settlement charges exceed the 10 percent tolerance. The appendix to RESPA's regulations would contain the closing script form, as well as detailed instructions and examples a settlement agent would use to complete the document.

D. Average Cost Pricing

In addition to proposing modifications to actual disclosure forms required under RESPA, HUD's proposed rule targets other aspects of the act to provide clarity and decrease settlement costs for consumers. One such modification would allow lenders and mortgage brokers to use average cost pricing for settlement services, rather than charge the consumer the exact cost in every circumstance. HUD would allow a lender to determine average cost by using the actual average cost of a settlement service over the previous six-month period or a tiered pricing approach. If a lender or broker uses one of these methods, HUD will deem the lender to have complied with the requirements of the rule for stating the actual charge.

E. Negotiated Discounts

Section 8 of RESPA prohibits any person from giving or receiving a thing of value in return for the referral of business. As currently defined, “thing of value” includes discounts, and Section 8 prohibits the giving or receiving of discounts in exchange for the referral of settlement service business. The rule, however, proposes to amend the definition to exclude discounts negotiated by settlement service providers (i.e., title companies) in the price of a third-party settlement service, as long as no more than the discounted price is charged to the borrower and disclosed on the HUD-1.

F. Required Use

Currently, RESPA’s regulations prohibit the required use of a particular settlement service provider; however, discounts, rebates, or customer incentives do not constitute required use as long as the rebate or incentive is a true discount that is not made up elsewhere in the transaction. HUD’s rule proposes to modify this definition of “required use” to include both economic incentives and disincentives that are contingent on a borrower’s use or failure to use a particular provider of settlement services. If, however, a settlement service provider offers an optional combination of services at a lower price, these discounted services would not constitute required use. This modification appears to be a direct result of complaints the department has received concerning home builders’ offers of large discounts to their customers who agree to use affiliated mortgage or title companies.

G. Miscellaneous Amendments

In addition to the extensive modifications discussed above, the rule proposes to update mortgage servicing disclosure requirements and remove expired provisions of the escrow regulations. The rule also would amend RESPA’s regulations to recognize the applicability of ESIGN, which would allow disclosures in electronic form. Consumers would be required to consent to the electronic receipt of documents, and a lender must ensure it meets all other ESIGN requirements.

FINDING ANSWERS TO ALL YOUR QUESTIONS HAS NEVER BEEN EASIER!

Who is the current successor to this lender?

Who services this mortgage?

How do I contact this lender?

Where do I request Payoff Statements?

Can I fax my request?

Are there any upfront fees?

Changes to lender names, phone numbers and addresses can lead to hours of searching for the correct lenders, departments and contact numbers for the loans you are paying off or need to clear from title.

www.PayoffAssist.com puts a stop to endless searching. With our database of thousands of mortgage lenders and servicers, all the information you need is at your finger tips.

– Successor / name change information
– Current phone numbers and fax numbers for the mortgage department
– Mailing addresses
– Payoff policies and fees

Whether you’re looking for the right lender to payoff an existing loan or need to track down the successor for a loan still outstanding on title, look no further than **www.PayoffAssist.com**.

FOR MORE INFORMATION ON OUR SERVICE AND A FREE TRIAL OFFER, VISIT WWW.PAYOFFASSIST.COM TODAY.

II. Potential Impact on Title Insurance Industry

Overall, the proposed modifications discussed above give every settlement service provider something to be concerned about. For the title insurance and settlement industry the newly proposed closing script is likely to get the most attention, and it raises several issues.

- First, the closing script would require a title agent to explain loan terms and settlement charges to the consumer, which, in many states, is a role that a licensed attorney is required to perform. In these states, if HUD requires a title or settlement agent to be responsible for explaining the loan terms to a borrower at closing, the agent could risk committing the unauthorized practice of law.
- Second, HUD acknowledges in the appendix to the rule that the addition of the closing script to the settlement process will increase the time it takes to conduct a real estate closing by approximately 45 minutes and increase the cost of a settlement by at least $54. HUD, however, does not appear to anticipate the additional time it will take to provide answers to borrower questions or give weight to the fact that title and settlement agents will be required to update software and train employees, which only adds to the extra expense. HUD states that its purpose for the rule is to simplify the process and reduce consumer costs, but the proposed closing script may have the opposite effect.
- Third, the rule does not provide answers to several practical problems with the closing script. For instance, if final settlement charges exceed the 10 percent tolerance,

The “Rules” of Rulemaking

Following is a synopsis of the rulemaking process by which federal agencies create new regulations or amend existing ones—

Regulatory agencies create regulations according to rules and processes defined by the Administration Procedure Act (APA). The APA defines a “rule” or “regulation” as:

The whole or a part of an agency statement of general or particular applicability and future effect designed to implement, interpret, or prescribe law or policy or describing the organization, procedure, or practice requirements of an agency.

And, the process of “rulemaking” is defined as:

Agency action which regulates the future conduct of either groups of persons or a single person; it is essentially legislative in nature, not only because it operates in the future but because it is primarily concerned with policy considerations.

Under the APA, agencies must publish all proposed new regulations in the Federal Register at least 30 days before they take effect, and they must provide a way for interested parties to comment, offer amendments, or to object to the regulation.

Some regulations require only publication and an opportunity for comments to become effective. Others require publication and one or more formal public hearings. The enabling legislation states which process is to be used in creating the regulations, and those requiring hearings can take several months to become final.

New regulations or amendments to existing regulations are known as “proposed rules.” Notices of public hearings or requests for comments on proposed rules are published in the Federal Register, on the Web sites of the regulatory agencies, and in many newspapers and other publications. The notices will include information on how to submit comments or participate in public hearings on the proposed rule.

In addition, the complete text of all proposed rules is published in the Federal Register and typically posted on the agencies’ Web sites.

Once a regulation takes effect, it becomes a “final rule” and is printed in the Federal Register, the Code of Federal Regulations (CFR), and usually posted on the Web site of the regulatory agency.

The RESPA proposal was released on March 14, 2008, with an open comment period until May 13, 2008. (ALTA requested a 60-day extension and it was unknown as of this writing whether it would be granted). HUD will review all public comments and amend its proposal, simply respond to comments, or seek further clarification. It can then release an amended proposed rule for comment or a final rule that may or may not contain changes. The final proposal is then submitted to the Office of Management and Budget for approval before becoming effective. Once passed, HUD has indicated that there will be a 12-month period to move to the new forms and regulations.

– Ed Miller, *Chief Counsel & Vice President of Public Policy*

should a settlement agent close the loan when he/she knows the loan is in violation of Section 5 of RESPA? If a closing agent must read aloud the closing script to a borrower, what does the closing agent do in escrow closings, internet closings, and closings by mail where there is no face-to-face meeting? What if the borrower does not speak English; must the closing script be read aloud or provided in writing in another language?

We expect that these are only a few of the issues the title industry will raise with HUD in connection with the proposed closing script.

> No other insurance agents (i.e., homeowners, auto, and life insurance) are required to disclose the percentage of insurance premiums they receive as compensation."

With regard to the proposed HUD-1, this form includes two additional disclosures that the Department does not propose for the GFE. In lines 1113 and 1114 of the new HUD-1, a title/closing agent would be required to disclose the title agent's portion and title underwriter's portion of the total title premium. Yet, in the Appendix to the rule the department expressly states that it removed the premium breakout from the GFE, as the title agents argued that itemizing the premium split is costly and serves no useful purpose. If this is the case, then what useful purpose does the disclosure serve on the HUD-1? No other insurance agents (i.e., homeowners, auto, and life insurance) are required to disclose the percentage of insurance premiums they receive as compensation. Moreover, if the disclosure of the agent and underwriter portions of the title premium is intended to allow the consumer to negotiate a different title rate, the disclosure of this split just one day prior to closing is too late to allow a consumer to shop for another provider.

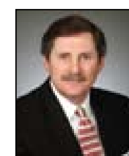
Finally, certain aspects of the proposed rule may disproportionally affect a title insurance or settlement agent's ability to offer the lowest prices to their customers. Notably while the rule allows for average cost pricing, the text refers to the determination of the average cost based on activities of the "loan originator." By using this specific term, one has to question whether only lenders and mortgage brokers may use an average cost for the settlement services they control. If this is the case, HUD fails to recognize that title and settlement agents would greatly benefit from the ability to use average cost pricing, particularly as it relates to mortgage recording fees. Because of the uncertainty of recording fees prior to closing, an average cost could help ensure that consumers do not pay more than actual recording fees, and the title or settlement agent is not at risk for claims of overcharges under RESPA.

Ultimately these items only skim the surface of the issues and impracticalities raised by the proposed RESPA rule. While the closing script appears to have the most impact on the title insurance industry, other aspects of the rule could make it more difficult, for instance, for title companies to compete with lender-owned affiliated business arrangements as well as negotiated discounts offered by lenders and other settlement service providers. As a result, the title industry should not assume this rule is for lenders only; your business could be directly affected by HUD's proposed changes.

III. Conclusion

Despite HUD's stated purposes for the proposed RESPA rule, the department has delivered a complicated rule that will prove to be controversial. Every corner of the settlement service industries likely will raise an objection to some piece of HUD's proposals. For the title insurance industry, the proposed closing script and limitations on average cost pricing likely will be hot issues that will elicit a strong response from title and settlement agents. Moreover, with the market in the midst of a credit crunch, one must question why at this particular time HUD would create new consumer disclosures that will require providers to expend considerable time and money to update necessary systems and train employees. Buckle your seatbelts; it's RESPA reform time, and that means déjà vu all over again.

For current information on RESPA go to *www.alta.org/publications/titlenews*.



Phillip L. Schulman is a partner with the Washington, D.C. office of the law firm of K&L Gates. He specializes in real estate and consumer finance matters affecting the title insurance, mortgage banking, and real estate industries.

We know this stuff inside and out.

For your next commercial real estate transaction, come to LandAmerica. Our experts know every aspect of the business from the inside out. LandAmerica Commercial Services has the special knowledge to handle your most complex transactions anywhere in the world, all from a local office. So you'll have accurate, complete and timely transactions every time. For your next transaction, count on LandAmerica to cover all the ins and outs.

Dedicated expertise.

Title and Escrow | Property Condition and Environmental Assessments | Valuations | Surveys
Zoning | Tax and Flood Services | UCC Insurance | 1031 Exchange Services | International Services
Construction Disbursement and Monitoring Services | TIC Services

866-442-3011 | www.landam.com/commercial
©2008. LandAmerica is a registered trademark of LandAmerica Financial Group, Inc.