


# Mortgage Origination:

*The Impact of Recent Changes on  
Homeowners and Businesses*

**House Financial Services Committee**  
*Subcommittee on Insurance, Housing and Community Opportunity*

Wednesday, July 13, 2011  
2:00 P.M.

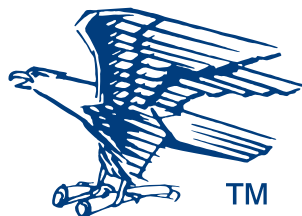
  
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ASSOCIATION





My name is Anne Anastasi and I am the President of Genesis Abstract, LLC in Hatboro, Pennsylvania. I have been in the land title insurance industry for 33 years, and I hold Pennsylvania's Certified Land Title Professional designation, which is the highest designation available in the title industry.

Currently, I serve as the President of the American Land Title Association. ALTA, founded in 1907, is the national trade association and voice of the real estate settlement services, abstract and title insurance industry. ALTA's over 3,800 member companies operate in every county in the country, where we search, review and insure land titles to protect consumers and mortgage lenders who invest in real estate. ALTA members serve as independent, third-party facilitators of real estate transactions. We do not represent the borrower, lender, seller or any other party in a transaction. ALTA members include title insurers, title agents, independent abstracters, title searchers, settlement agents and attorneys, ranging from small, one-county operations, to large, national title insurers.

On behalf of ALTA, I appreciate the opportunity to appear before you today to discuss mortgage origination issues. My testimony will focus on the very end of the mortgage origination process, the closing. At closing, ALTA members serve as the independent, third-party facilitators of the real estate transaction. It is in this role that ALTA members are called upon for two major purposes. First, we ensure that the transaction is closed quickly, honestly and in accordance with all the parties' instructions. Second, we serve as the last resource for consumers when they have questions about their transaction.

As we seek to improve the mortgage origination process, we need to fundamentally rethink a key part of the architecture of the current process: federal mortgage disclosure laws. These laws are primarily designed to help consumers shop for mortgage and settlement services by providing them with timely information about their transaction. While this goal is laudable, from our vast experience at the closing table, the execution reveals some shortcomings that actually cause confusion and may be counterproductive for consumers.

## **Overview of Closing Process**

When an individual participates in a closing to buy, or sell a home or refinance their mortgage, the main reason that such a complex real estate transfer can be quickly accomplished is because an independent, third party professional has already pulled together all of the documentation necessary to close the transaction. The closing process differs state by state and in some cases county by county, but the outcome is roughly the same in every jurisdiction.

Closing – or settlement as it is known in some parts of the country — is a term used to designate the point in time at which the contemplated transaction is concluded. For most residential purchase and sale transactions, closing generally designates the point at which title to the property is transferred from seller to buyer, a mortgage (or "deed of trust") is given by the buyer/borrower to the lender and the funds from the buyer and lender are transferred to the seller. The closing date is typically negotiated between the buyer and the seller along with other terms when they agree to a purchase contract.

Once a closing date is selected, the parties will select a closing or settlement agent. Consumers can shop around to select a settlement agent to perform the closing functions, or they can rely on a recommendation from their real estate agent or lender. While variances occur throughout the country, a closing agent is typically an attorney, or an employee of a title company, or escrow company. The closing agent acts as a clearinghouse collecting all the necessary documentation, including the deed, mortgage, title and homeowners insurance policies, payoffs (if there are liens on the property that must be released) and pest inspection reports. This person also handles the exchange of monies, including any earnest money deposit, mortgage funds and personal funds of the parties. Lastly, the closing agent prepares the Settlement Statement. The HUD-1, as it is referred to, documents all costs for both the buyer and seller associated with the closing and is required to be issued on all federally-related mortgage transactions.

At closing, the property is transferred from the seller to the buyer. In most parts of the country, consumers will sign a number of documents whose content will be described by their closing agent. Finally, the settlement agent will forward payment to any previous lender, other lien holders, tax collectors, municipalities and pay all of the other parties who performed services in connection with their closing, pay out any net funds to the seller, and order a final search of the title to their new home before finally recording all of the documents needed to complete their purchase.

This process can be daunting, but thanks to the efforts of closing agents and the American property rights recording system, transactions are most often closed in 30-45 days after signing the purchase agreement. It is worth highlighting that the United States enjoys one of the fastest transaction times in the world due to this public private partnership.

### **The Federal Disclosure Regime**

In 1974, Congress passed the Real Estate Settlement Procedures Act. In Section 1 of RESPA, Congress declared that, "significant reforms in the real estate settlement

process are needed to insure that consumers throughout the Nation are provided with *greater and more timely information on the nature and costs of the settlement process* and are protected from unnecessarily high settlement charges caused by certain abusive practices that have developed in some areas of the country.” (emphasis added) A similar sentiment was expressed when Congress passed the Truth in Lending Act in 1968<sup>1</sup>.

For mortgage transactions, these Acts mandate a two part regime of providing consumers with an early disclosure and a late disclosure of loan and settlement costs. This regulatory requirement has fundamentally shaped how mortgages are originated today.

Within three days of applying for a mortgage, consumers receives two disclosures: 1) an estimate of their loan terms and 2) an estimate of the closing costs (called the Good Faith Estimate or “GFE”). These documents are designed to help consumers shop for their mortgage by giving them estimates of their mortgage and closing costs that they can compare between competing lenders. On the current Good Faith Estimate, HUD includes a “shopping chart” to help assist consumers in comparing mortgage offers. However, despite the focus on consumer shopping, these early disclosures often are insufficient to help consumers shop because the form masks certain charges by reflecting only a combined cost number for several services, or “roll-up,” which ultimately makes it more difficult for consumers to shop effectively for individual services.

After picking a loan product, consumers receive final disclosures at the closing table which outline the actual loan terms and the final closing costs called the Uniform Settlement Statement or HUD-1. Recent reforms have turned the HUD-1 from a simple disbursement sheet outlining all the fees paid at closing into a comparison document to help consumers compare their GFE and HUD-1 to assess the accuracy of the estimate and ask informed questions about whether costs changed and, if so, why they changed.

While these are the main disclosures given to consumers, other federal, state and local laws require that consumers be provided a myriad of additional disclosures at closing.

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<sup>1</sup> “The Congress finds that economic stabilization would be enhanced and the competition among the various financial institutions and other firms engaged in the extension of consumer credit would be strengthened by the informed use of credit. The informed use of credit results from an awareness of the cost thereof by consumers. It is the purpose of this subchapter to assure a meaningful disclosure of credit terms so that the consumer will be able to compare more readily the various credit terms available to him.” 15 USC 1601(a).

## **Policy Recommendations**

In conducting closings, ALTA members find that consumers benefit most from disclosures that provide them with tools to more fully understand their individual transaction. ALTA would like to make the following recommendations to improve federal mortgage disclosures to ensure consumers receive the information needed for them to shop for their mortgage and settlement services.

### **Disclosures should be transparent so that consumers can get a complete view of their transaction**

Improving transparency by itemizing costs will help consumers understand their entire transaction. One significant change to the RESPA disclosures adopted in November 2008 and implemented in January 2010 was the introduction of “roll-up” lines and aggregate line item totals on the HUD-1 Settlement Statement. This concept was designed to help consumers shop for settlement services by making it simpler to aggregate classes of charges. While the stated goal was improving consumer understanding of charges, roll-ups have not been an effective tool for achieving this goal. Rather, our experience has found that transparency, simplicity and itemization of charges is a more effective solution for consumers.

In the current forms, roll-ups lump fees into aggregate standard categories. Consumers are then encouraged to shop based on these aggregates. Alongside or underneath the aggregate, some (but not all) fees are itemized. Thus, consumers are given a disclosure that includes an aggregate fee that may not reconcile with an addition of the itemized fees listed underneath or alongside.

ALTA members routinely see the confusion this causes for consumers who are unable to reconcile the numbers on the page. A better solution would be to return the itemization and transparency from the previous GFE and HUD-1. Just like when you go out to dinner, your check doesn't just give you a total price. Rather, each item is listed giving you a breakdown of what you pay for. These forms would allow consumers to see where their money is going and to better inquire regarding fees they find questionable.

Itemization would also help consumers shop. Greater transparency of the source of costs helps consumers see what costs are included in the cash needed to close. This level of transparency offers a better opportunity for consumers to shop for these additional services by providing them detailed information to use when going to other providers to obtain competing bids. This level of detail and transparency promotes competition among providers, thus avoiding excessive fees and promoting a realistic picture of the transaction. Finally, this level of detail promotes consumer education by

allowing consumers to look inside their transaction and have a better understanding of the fees they incur for various services.

**Disclosures should include accurate estimates so consumers can make informed decisions about their transaction**

Consumers' ability to shop for their mortgage and settlement services is improved when the estimates provided are accurate. However, we have found that attempts to tie initial estimates to final costs through the use of tolerances have not resulted in consumers receiving accurate estimates.

Currently, two categories of fee estimates are subject to restrictions on their increase from the numbers originally shown in the GFE. The first, which includes a lender's own charges and government transfer taxes, may not increase by any amount at closing. This category is often referred to as "zero tolerance". The second category includes services required by the lender where the provider is not selected by borrower lender. These costs, in the aggregate, may not increase by any more than 10% at closing. Should costs increase in excess of the tolerance allowance, a payment must be made by the lender of the amount in excess of the allowed tolerance.

While designed to provide more accurate disclosures, tolerances have had the opposite effect. To avoid a tolerance violation, some providers overestimate fees within their control that are subject to tolerance. These overestimations allow providers to ensure that even if some fees outside of their control increase, there will be a sufficient buffer to prevent a tolerance violation. Even if a tolerance violation occurs, many consumers express surprise at the prospect of the refund, and show no understanding of the tolerance concept.

Another way that some providers avoid tolerances is by issuing multiple initial disclosures during the transaction. Since only the most recent GFE is disclosed to the settlement agent for the computation of tolerances, these "magic GFEs" (as they are called in the industry) typically appear numerous times throughout the process to update the estimates to avoid a violation. The volume and frequency of the issuance of these "magic GFEs" (even though currently either prohibited or severely restricted by current RESPA regulations) have led some consumers to admit to ALTA members that they do not even open the new disclosures that they receive.

The effect of these practices is that tolerances are not necessarily resulting in more accurate estimates at the time of application or improved consumer comprehension. Thus, they fall short of their intended purpose.

## **Regulators should consider the impact new or altered disclosures will have on actual closings instead of isolated interviews with consumers**

While disclosures represent only a small fraction of the documentation presented at closing, they are one of the few parts of the process that is growing. In my home state of Pennsylvania, a typical closing package includes 60-75 pages of documents. Each one of these documents must be reviewed with the consumer before they sign them at closing. This can be a time consuming process and usually ends with the consumer having a sore wrist and confused mind.

This whirlwind of documents may also have a negative impact on consumers. As a closer, I frequently deal with consumers who, in the face of the stack of documents they need to sign, simply give up and sign without taking the time to understand the contracts and obligations that they sign. Better efforts should be made to ensure that ever increasing government disclosures actually help consumers rather than hinder their understanding of their transaction.

To achieve this, qualitative testing of disclosures must take place in the context of the greater transaction to ensure that policymakers grasp the true impact that these forms have on consumers' understanding of their transactions. During the last round of RESPA Reform in 2002-2009, consumer testing took place in a vacuum where the testing of the GFE and HUD-1 done individually instead of as part of a greater transaction. While the new forms passed that testing, many ALTA members find that consumers are having a more difficult time, rather than a less difficult time understanding their costs.

At closing, typically four federally-required disclosures are provided to the consumer: the HUD-1, the Truth in Lending Disclosure, the Itemization of Amount Financed and the Lender's Right to Transfer Servicing Rights. These documents are all intended to inform consumers about the specific aspects of their transaction.

Since these disclosures have a common goal, Congress has repeatedly asked regulators to attempt to combine these disclosures into a single document. However, this task has proven daunting since many of the underlying federal statutes and regulations have differing terms, definitions and timing requirements. These divergent structures make integration challenging. Greater efforts need to be taken by regulators and Congress if necessary, to combine disclosures and reduce the amount of paperwork required at closing.



## **Nationally mandated disclosures should be flexible enough to allow for variation to reflect the consumer's individual transaction**

As the saying goes, all real estate is local. Unfortunately for consumers, federal mortgage disclosures do not take this axiom into account. While real estate closings and practices vary greatly across the country, HUD in its 2010 RESPA rule created a regime that forces transactions into a one-size-fits-all disclosure.

This was not always the case. Originally, RESPA disclosures allowed for some variation for local custom. In states and localities where custom does not follow the norm, these national disclosures make it more difficult for consumers to shop for, and understand the settlement services that they receive.

### **Disclosures should be flexible enough to account for regional variations in closing practices**

There are a number of fees listed on the GFE and HUD-1 that, in large swaths of the country, are paid for by the seller instead of the buyer in the transaction. Despite this, the latest RESPA reform included strict requirements that ALTA members and other settlement agents list these fees as being paid by the buyer (with appropriate credits given on other lines). At closing, the closing agent must explain this structure to confused consumers.

One example of this paradox is Owners Title Insurance. In many parts of the country, including Southern California, Owners Title Insurance is paid for by the seller by custom or negotiation. However, the closing agent must disclose the policy as a charge paid by the buyer on the HUD-1. This causes confusion for the consumer, and must be explained at closing to the consumer. Other examples include certain real estate taxes, home warranties and inspections.

### **Make disclosures fit the transaction, not the other way around**

Mortgage disclosures need to be flexible enough to disclose all transaction costs. However, the current HUD-1 is too rigid and strictly controls where fees may be disclosed and the number of lines in each category. This leads to many fees being either left off the form or disclosed on an addendum, making it harder for consumers to see their entire transaction. Greater effort should be undertaken to ensure that all fees in a certain category are shown in concert on the disclosure.

## **Disclosures should encourage consumers to make informed decisions about closing services**

At a minimum, federally-mandated mortgage disclosures should not prejudice consumers against protecting their financial investment. Certain services purchased as part of the real estate transaction protect consumers' financial interests. Federally-mandated disclosures should encourage consumers to investigate whether the service is in their best interest.

The choice of words used to refer to certain services can greatly influence consumers' likelihood of purchasing those services and acting in their best financial interests. Against Owners Title Insurance serves as good example. Recent proposals use the term "not required" on the GFE to disclose to consumers the closing costs that are not mandated by the lender, but are available to consumer, including Owners Title Insurance. However, by calling a service "not-required," these proposals contain a less than encouraging implication that the service is of less value to consumers. This message prejudices consumers against considering these services, even when these services are often in consumers' best interests and protection.

ALTA strongly encourages policymakers to avoid using the term "not required" in these disclosures, and instead use terms like "recommended" or "advisable". These terms encourage consumers to investigate services like owner's title and make an informed decision. This concept was recognized by HUD in the current Settlement Cost Booklet where the guide encourages consumers to investigate these services, including an Owners Title Insurance policy, indicating: "If you want to protect yourself from claims by others against your new home, you will need an owner's policy." If we have learned anything from the foreclosure crisis, it is that consumers should be encouraged to investigate products like Owners Title Insurance that help protect the consumers' interest.

## **Timely disclosures help consumers make informed decisions about their transaction**

Finally, ALTA members have found that disclosures will only be effective if they are timely. Currently, consumers have a right to request their HUD-1 up to 24 hours in advance of closing. However, in practice, few if any consumers are able to obtain their disclosure that early in the process. Delays in transmitting the lender's closing instructions and other documents not only prevent the consumer from receiving the HUD-1 in advance of closing, but also force the consumer to wait at the closer's office (often times with the moving truck outside) while the closing agent waits to receive these documents and rushes to complete the HUD-1.

Consumers would be better protected if they received their closing documents in advance of their closing. This added transparency would allow consumers to read through their closing documents before having to sign them. It would also improve consumers' understanding of the documents, as they would be able to take the forms to a trusted advisor for explanation. Lastly, it would allow consumers to review the terms to ensure that they are paying the correct amount they were quoted.

## **Conclusion**

ALTA appreciates the opportunity to discuss our firm belief that one of the best ways to improve the mortgage origination process is to improve federally mandated mortgage disclosures. We strongly believe that consumers are best protected when they are able to make informed decisions about their transaction based on transparent and accurate information. ALTA is eager to serve as a resource to the Subcommittee and other stakeholders, and I am happy to answer any questions. Thank you.