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HEARING BEFORE THE

U.S. HOUSE OF REPRESENTATIVES COMMITTEE ON FINANCIAL SERVICES SUBCOMMITTEE ON OVERSIGHT & INVESTIGATIONS

ENTITLED

HUD'S PROPOSED RESPA RULE

WRITTEN TESTIMONY OF

T. ANTHONY LINDSEY

ON BEHALF OF THE

NATIONAL ASSOCIATION OF REALTORS®

SEPTEMBER 16, 2008

INTRODUCTION

On behalf of 1.2 million members of the National Association of REALTORS® (NAR), I am pleased to provide comments to the United States House of Representatives Committee on Financial Services Subcommittee on Oversight and Investigations concerning the proposed rule[1] of the United States Department of Housing and Urban Development (HUD) to amend the Real Estate Settlement Procedures Act (RESPA) Regulation X. The proposed rule is intended to simplify and improve the disclosure requirements for mortgage settlement costs and to protect consumers from unnecessarily high settlement costs by eliminating kickbacks and referral fees.

The National Association of REALTORS® is America's largest trade association, including five commercial real estate institutes and its societies and councils. REALTORS® are involved in all aspects of the residential and commercial real estate industries and belong to one or more of some 1,500 local associations or boards, and 54 state and territory associations of REALTORS®.

REALTORS® have a strong stake in seeing that consumers are provided high value products and services, competitive choices, and simplified disclosures of mortgage settlement costs early in the loan transaction because:

- Real estate agents are typically the first contact in the home buying process, develop close working relationships with clients, and stay with the consumer through settlement. As a result, consumers look to real estate professionals to help them understand the home buying process from beginning to end.
- Abusive lending practices are most likely to occur when consumers are overwhelmed by a transaction laden with unfamiliar financial terms and a confusing array of compensation models and settlement services and cannot shop for competitive rates and high value products and services.
- Early disclosures, clearly presented, will help consumers identify the mortgage product and settlement services which provide the optimal combination of cost and value for their particular circumstances.
- Thorough disclosures that use similar structure and terms in the closing documents will make it easier for consumers and their representatives to identify changes and previously undisclosed charges.

HUD has received nearly 12,000 comment letters on the proposed rule which has now been revised and was sent to the Office of Management and Budget (OMB) for final review on August 21, 2008. OMB has up to ninety days to complete its review of the rule. In light of the fact that HUD utilized only 50 work days to study 12,000 comment letters and revise the proposal, NAR is concerned that some easy "quick fixes" were applied and that there is little likelihood that several critical content and design problems could have been thoughtfully

[1] 73 Fed. Reg. 14030 (March 14, 2008); Real Estate Settlement Procedures Act (RESPA): Proposed Rule To Simplify and Improve the Process of Obtaining Mortgages and Reduce Consumer Settlement Costs.

considered and resolved in just over two months.[2] NAR's formal comment letter was submitted to HUD on June 12, 2008 and discusses in detail NAR's concerns with the proposed RESPA rule.[3]

The focus of this written testimony will highlight those aspects of the rule that have become, through further study and discussion since the close of the comment period, the major points that NAR believes must be addressed before a final rule is implemented. These points are as follows:

1. HUD's Good Faith Estimate Fails to Achieve Its Objectives
2. HUD's Anti-Competitive Pricing Mechanisms Will Hurt Consumers
3. HUD's Economic Analysis is Flawed

HUD's GOOD FAITH ESTIMATE FAILS TO ACHIEVE ITS OBJECTIVES

The Right Balance Between Simplification and Clear Disclosures Has Not Been Achieved

One of the primary objectives of the RESPA statute is to provide clear disclosures so that homebuyers will better understand settlement costs. NAR supports many of the good intentions HUD has brought to the process, which resulted in an improved appearance of the Good Faith Estimate (GFE) and the translation of complex financial information into language consumers will understand. But HUD has not found the right formula for determining what information to include and how to present it.

This view is widely shared not only by industry, but by other agencies of the government which have called for additional testing and development in order to find the right balance between simplification and disclosure[4]. The calls for additional testing from industry and other federal agencies are based on the unsound testing methodologies employed by HUD. For instance, testing the "closing script" on only ten people in only one round of testing is hardly an appropriate method on which to base an expensive structural change to the settlement service industry.[5] As a result, NAR strongly believes that HUD's proposed disclosure provisions need to be thoroughly tested and improved before they are finalized.

In addition, RESPA directs HUD to regulate disclosures on settlement costs while the Truth in Lending Act (TILA) directs the Federal Reserve Board to regulate disclosures on loan terms. This has resulted in separate disclosures by the two agencies which have proven to be

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2 HUD did not work with industry or announce its changes to the proposed rule prior to submitting it to OMB. Consumers would be better served, and an improved final rule would result, if a comment period was provided for stakeholders to review changes made by HUD to the proposed rule prior to sending the final version to OMB.

3 NAR's comment letter is available at http://www.realtor.org/GAPublic.nsf/files/Letter_HUD_RESPA_GFE_06112008.pdf

4 See Attachment 3: excerpts from comment letters received by HUD calling for additional testing and coordination of disclosures from the Board of Governors of the Federal Reserve, Federal Deposit Insurance Corporation, Federal Trade Commission and the Small Business Administration Office of Advocacy.

5 See p. 145, Summary Report, Consumer Testing of the Good Faith Estimate Form (GFE), U.S. Department of Housing and Urban Development, Office of Policy Development and Research, February 2008.

uncoordinated, overlapping and inconsistent. As a result, the two sets of disclosures emanating from the Federal Reserve Board and HUD are confusing to consumers. This problem has been recognized by Congress since 1996 when it first requested the Federal Reserve Board and HUD to engage in joint rulemaking under TILA and RESPA to harmonize the two sets of disclosures. To date, the two agencies have not undertaken this common-sense task despite repeated requests from Congress and with the knowledge that the existing set of separate disclosures is a primary cause of consumer confusion.

It is critical that HUD work with the Federal Reserve Board to harmonize RESPA disclosures with required Truth-In-Lending Act (TILA) disclosures. Harmonization is necessary to make sure the consumer is not confused by two different sets of disclosures which cover some of the same information and which could be interpreted as being inconsistent with one another.

NAR believes that the current proposal could have been greatly improved if HUD had collaborated with industry and consumer groups – as well as the other federal banking agencies - during the past three years since HUD's RESPA Roundtables in the summer of 2005. Unfortunately, HUD chose not to do so. Instead, it added new provisions never before seen by consumers or industry, rolled them into a complex 96-page regulation and then cut in half a Congressional request to extend the comment period. NAR believes that HUD must take the time required to simplify, coordinate and properly test the new disclosure provisions and include stakeholders in the process if it is to accomplish the goal of better consumer understanding of mortgage and settlement costs.

The GFE is Too Long and its Format Does Not Match the HUD-1

NAR believes the proposed four-page GFE will serve as a psychological barrier to many consumers who will be baffled by four pages of data, fine print and instructions. It is unclear whether consumers will understand (or have the time and inclination to learn) the system proposed for the disclosure of discount points and yield spread premiums (YSP)[6] and the underlying economic incentives that play into these industry compensation models. NAR urges HUD to employ sound testing methodology in conducting further testing on its proposed disclosure models.

NAR also believes it is imperative that the consumer have, at some point, access to <u>all</u> relevant cost information. HUD's decision not to include all costs in its revised GFE will result in consumers getting less than the full disclosure Congress intended in the original statute.[7] While HUD's stated intent in not itemizing all charges is to eliminate junk fees, the result will be just the opposite as the change creates the opportunity to hide additional, undisclosed fees into "packages" to the detriment of consumers.

6 A recent FTC study recommended that the YSP and "points" not be disclosed they are too confusing to the consumer. (Comments of the Staff of the Bureau of Consumer Protection, the Bureau of Economics, and the Office of Policy Planning of the Federal Trade Commission, April 8, 2008, In the Matter of Request for Comments on Truth in Lending, Proposed Rule, Docket No. R-1305, pp 14-15)

7 "Each lender shall include with the 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." 12 USC 2604(c) *emphasis added.*

Despite the suggestion of its own design consultants and a broad consensus of industry and consumer groups, HUD did not reformat the GFE to match the look of the HUD-1 – a common sense design change that should have been a primary focus of reform. NAR believes this change would greatly assist consumers in understanding whether or not the terms and expenses that were disclosed to them at loan application are those that are the governing terms and costs at closing. It would also obviate the need for the cumbersome and expensive "closing script" that provides information too late in the process to be useful to consumers.

Matching formats for the GFE and HUD-1 statement have been advocated by a number of organizations for some time now. NAR, along with the Center for Responsible Lending, recommended to HUD two years ago that it provide consumers with a one-page summary GFE for shopping purposes, accompanied by a full GFE designed to mirror the format of the HUD-1.

HUD'S CHANGES WILL PROVE ANTI-COMPETITIVE AND WILL HURT CONSUMERS IN THE LONG-RUN

The proposed rule attempts to lower settlement costs through, what in the end is, a government-designed pricing system for closing costs.[8] Provisions on volume discounts and price tolerances, as structured by HUD and embedded in the GFE, will permanently favor large financial institutions but only temporarily benefit consumers. HUD's pricing schemes will reduce competition and promote the concentration of settlement service providers, discourage innovation, reduce the quality of services provided to consumers and ultimately lead to higher closing costs. As we have seen in the ongoing crisis in the mortgage industry, the concentration of economic power in the hands of the privileged few benefits no one.

More specifically, HUD's proposed GFE allows lenders to offer consumers a package of lender-preferred settlement services such as title search, title insurance, appraisals and inspections. The natural consequence of this proposal is that the largest lenders will best be able to apply considerable market pressure on settlement service providers to reduce their prices in order to be included in the lenders'preferred packages. Alternatively, large lenders could price their own in-house or affiliated providers' services below cost simply to acquire market share. While this economic behavior might benefit consumers in the short term, NAR believes that the long-term effect will be to drive small providers out of business followed by an inevitable rise in closing costs once competitors are eliminated.

Consider the following scenario:

> Mr. and Mrs. Homebuyer are presented with a lender-preferred package of settlement services from a large mortgage lender. The Homebuyers are told by the lender that it has done the shopping for them by utilizing its size and market influence to extract significant concessions in the form of volume discounts from its preferred providers.

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[8] RESPA, which specifically calls for lowering closing costs through the elimination of kickbacks and referral fees was never intended to be rate-setting statute and lacks any language authorizing HUD to impose pricing systems.

> Next, the lender points out to the Homebuyers that the GFE guarantees the lender's prices in its package. It is emphasized that if the Homebuyers still want to look for their own settlement providers, they can do so, but that the lender will not guarantee the prices of the Homebuyers' providers which could double or triple at closing. The lender concludes by informing Mr. and Mrs. Homebuyer that if they want to select their own providers, they'll also have to pay for another GFE.

Under this scenario, many harried borrowers, already mystified by the entire process and the four-page GFE, may easily be talked out of researching additional companies and will accept the lender's argument that they did the shopping for them. The advantages of sticking with the lender and his preferred choices, such as ostensibly reduced settlement costs through volume discounts and elimination of the risk of dramatic price increases at closing will be persuasive. Futhermore, the borrowers won't have to pay for another GFE.

But there will be unwanted costs to this approach. Clearly, larger lenders will be in the best position to negotiate favorable terms from third party service providers compared to smaller mortgage banks and other settlement service providers. Large lenders will also prefer to work with the larger settlement service providers able to handle the volume generated by a large lender and to reduce administrative costs and risk. Small, local firms, unable to reduce prices or unwilling to reduce the quality of services necessitated by steep price concessions, will be left out. As a result, both the mortgage and settlement service industries will move towards more concentration and thus less competition.

In addition to the anti-competitive nature of the proposal, HUD's pricing mechanisms ignore the importance of value and quality services in the real estate transaction. NAR believes most consumers do not shop for settlement services, or any other significant product based on price alone. Many consumers willingly pay more for the kind of enhanced services that ensures the job is done right and in a timely manner. However, when reduced costs are the focus, quality can suffer.

The current mortgage market crisis provides the best evidence needed to demonstrate that quality does matter. A thorough and professional appraisal offers assurance of the value of a property. The quality of a loan officer's review of a credit report can mean a borrower gets a better interest rate and/or the most appropriate loan for their circumstances. The quality of a title report helps ensure that the buyer has unencumbered ownership of the property purchased and that title risks to lenders and other parties in the transaction are minimized. Creating a system promoting the lowest cost providers as HUD has done with its government-directed volume discounts and price tolerances will favor large lenders and will squeeze quality and local experience out of the system to everyone's detriment. When competition is based on price alone, the chance that consumers will receive poor service and take on more risk increases.

The housing market does not need more "drive by" appraisals where the appraiser, in order to save money, doesn't even get out of car to inspect the home. It does not need loan officers who don't truly understand the differences among the array of mortgage products offered or cannot interpret a credit report so as to direct a consumer to the best mortgage for which they qualify. It does not need closing agents who don't know the customs and rules of the area in which they work.

If recent experience has taught us anything, it is that cutting corners in this business has led to shredded family dreams. The mortgages that have been most troublesome for consumers are the cheapest and easiest to close because they include no documents, no income verification and limited appraisals. The proposed rule, with its extra-statutory mechanisms to lower costs, will only encourage the kind of shoddy services that have resulted in so many inappropriate mortgages and the problems we continue to see in the mortgage and housing markets.

While NAR strongly supports HUD's interest in increased competition and lower prices, government's role should be focused on eliminating kickbacks as called for in the statute, and strong enforcement efforts.[9] HUD's attempt to achieve price reductions through manipulating pricing mechanisms is contrary to HUD's statutory charge, artificially distorts market forces, promotes low-quality settlement services that jeopardize the value of the underlying property and faith in the real estate transaction, and is not in homebuyers' best interest.

HUD's ECONOMIC ANALYSIS IS FLAWED

A. The Proposed Good Faith Estimate

Under the proposed rule, a guaranteed GFE will be required *prior* to loan application. While some components of closing costs are predictable, e.g. the origination fee, other components are not. These costs can change from day to day. Lenders will either have to hedge this risk, or issue a new GFE once an application has been received. Either approach will involve costs that are not considered in the HUD's estimates.

The Department states that it "hopes" that the four page GFE form – along with its accompanying guarantees – will be delivered to consumers free of charge. However, even if this occurs, lenders will undoubtedly seek to recoup their additional costs as part of the origination fee. Originators may also incur additional costs from preparing the GFE twice. In the end, such additional costs will almost certainly be passed through to the consumer.

In an economic critique of the proposed rule which points out a large number of shortcomings in HUD's economic analysis, Dr. Anne Schnare concludes, "[i]f, on the other hand, lenders decide to charge for the form, the GFE could actually *decrease* the amount of shopping that occurs– thereby negating the very benefits that the Department is attempting to achieve." [10]

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9 HUD has a poor record of responding to industry requests for clarification. See: Small Business Administration's 2007 Fiscal Year National Ombudsman Report to Congress made available August 25, 2008. The report gives HUD a grade of "F" for timeliness of responses (most agencies received grades of "A" or "B"). It is indicative of HUD's non-responsiveness that NAR sought guidance from HUD in July 2007 on series of RESPA compliance questions and received a partial response 13 months later in August 2008 which, for the most part, reiterated previous guidance and deferred responses to the main issues to other more formal means of providing guidance. On the more uncertain issues, therefore, NAR still has not received the requested guidance from HUD.

10 See Attachment 4: "The Estimated Costs of HUD's Proposed RESPA Regulations" by Dr. Anne B. Schnare, June 3, 2008, for an expanded analysis of HUD's proposed rule.

B. The Proposed Closing Script

HUD assumes that reading the closing script will take about 45 minutes of the closing agent's time, which would almost double the amount of time typically required to close a loan. While HUD calculates the cost of this requirement on the settlement agent's part, it makes no attempt to recognize the costs to the other participants at the closing table, including the borrower/buyer and the seller. This oversight could potentially multiply the projected "opportunity costs" by a factor of four or more, raising the projected cost per loan significantly.

The Department also fails to document the alleged benefits that flow from the closing script. By the time the borrower reaches the closing table, it is highly unlikely that he or she will walk away from the transaction unless serious misrepresentations or issues are uncovered. It is more likely that in cases where a variance exists, someone – the buyer, seller or the real estate agents – will reach into their pocket and pay for an excess that was the responsibility of the loan originator.

In addition, the proposal would have the closing agent act as the consumer's representative but without any ability to control the information being explained. Some have argued that the proposed changes would force the closing agent to assume the role of the "RESPA police." Aside from legal questions regarding whether closing agents, other than attorneys, can play such a role, the requirement would expose the closing agent to additional legal and regulatory risk, which would once again increase the cost of closing.

CONCLUSION

HUD's proposed rule doesn't achieve the objective of simplifying the closing process; distorts the market to the detriment of consumers by imposing anti-competitive pricing mechanisms; and underestimates the cost to industry and consumers alike. HUD's proposed rule imposes wholesale changes on the settlement service industry at a time when the troubled housing market can at least afford ill-conceived fundamental changes, inefficiencies, inequities and understated expenses which NAR believes will result[11]. With regard to costs, the proposed rule will require the industry to modify existing software programs, assume additional risks associated with mandated tolerance levels on the GFE, and provide additional services (e.g. closing script) that may be of dubious value to the consumer.

NAR believes in better disclosures of mortgage terms and third party settlement services to help consumers understand the products they are buying. NAR also supports the policy of ensuring a fair and competitive economic system. But we believe that HUD's RESPA reform proposal should be reworked to focus on common sense disclosures, coordinated with the

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11 HUD provided a 590-page economic analysis in support of the proposed rule. NAR's initial analysis indicates that HUD's estimates of costs are underestimated and that secondary negative effects on small businesses were not considered by HUD. The Department admitted that "a new business model is being put in place for the mortgage industry" but dismisses the issue by stating that "It is difficult to provide comments on a market structure that does not yet exist." (pp. 3-87 Economic Analysis). And, while the Department spends hundreds of pages justifying its estimates of consumer benefits, the reality is that any such benefits are extremely difficult to quantify.

Federal Reserve Board's Truth in Lending disclosures, while eliminating volume discount and tolerance provisions which are anti-competitive because they favor large lenders. It is not enough to simply strip out poorly conceived elements such as the closing script. The entire proposal must be reworked with a focus on meeting the statutory obligation of ensuring clear, concise disclosure of settlement costs.

On May 9, 2008, the White House Chief of Staff, Mr. Joshua Bolten, stated in a memorandum sent to the heads of all executive branch agencies:

> The President has emphasized that the American people deserve a regulatory system that … ensures a fair and competitive economic system …. We need to continue this principled approach to regulation as we sprint to the finish, and resist the historical tendency of administrations to increase regulatory activity in their final months. We must recognize that the burden imposed by new regulations is cumulative and has significant effect on all Americans…. Every regulatory agency and department has a responsibility for continuing to ensure regulations issued in this final year are in the best interests of the American public.

NAR couldn't agree more and we hope that HUD listened carefully to Mr. Bolten's good advice before submitting its final RESPA rule to OMB. NAR urges all stakeholders involved in this effort to put aside the time constraints of the political calendar and focus RESPA reform on well-tested, clear disclosures formatted to provide simple, clear, and relevant information to consumers and without artificial, anti-competitive pricing schemes. We have the ability to do RESPA reform right and consumers cannot afford another regulation carelessly imposed for political reasons.

Thank you for the opportunity to submit NAR's comments on the proposed rule to address improving disclosure of mortgage settlement costs.

Attachments:

Attachment 1: NAR Draft Summary Good Faith Estimate
Attachment 2: NAR Draft Full Good Faith Estimate
Attachment 3: Excerpts from agency RESPA comment letters.
Attachment 4: Dr. Anne Schnare's economic analysis of HUD's proposed rule.

Summary of Guaranteed Good Faith Estimate (Discussion Draft)

Name & Address of Borrower:	**Name & Address of Lender or Originating Company:**
Property Location:	**Date:**

LOAN TERMS

Interest rate: fixed ☐ adjustable ☐	**%**
If adjustable, maximum yearly increase **and maximum total increase**	**%** **%**
Loan Amount	**$**
Principal and Interest **Estimated Taxes** **Estimated Insurance**	**$** **$** **$**
Total Estimated Monthly Payment	**$**
If adjustable, maximum yearly increase **and maximum total increase** **$** **$**	
Loan Duration	**years**
If loan does not fully pay off, **amount still owed when loan ends**	**$**
Prepayment penalty: ☐ yes ☐ no	
How computed:	
Maximum amount:	**$**

SETTLEMENT CHARGES - Summary of Attached Good Faith Estimate

"Series" numbers correspond to line designations on the Good Faith Estimate and the HUD – 1 Settlement Form

Series 800 - Lender Fees: **(Origination fee, discount fees, etc.)**	**$**
Series 800 - Mortgage Broker Fee	**$**
Series 800 - Fees in Connection With Loan: **(Appraisal, Credit Report, Etc)**	**$**
Series 900 - Required Advance Payments: **(Advance interest, insurance, etc.)**	**$**
Series 1000 - Reserves (Escrow) Required at Closing: **(Property insurance and taxes, etc.)**	**$**
Series 1100 - Title Charges **(Title search, title insurance, attorney fees, etc.)**	**$**
Series 1200 - Government Fees **(Recording fees, taxes, etc.)**	**$**
Series 1300 - Additional Settlement Charges **(Survey, pest inspection, warranty, etc.)**	**$**
TOTAL SETTLEMENT COSTS – Cash Required at Closing:	**$**

Attachment 2: NAR Draft Full Good Faith Estimate

Guaranteed Good Faith Estimate (Discussion Draft)

Name & Address of Borrower:	Name & Address of Seller:	Name & Address of Lender or Originating Co.
Property Location:	Settlement Agent:	
	Place of Settlement:	Settlement Date:

Total Loan Amount: **Interest Rate:** **Term:**

Settlement Charges

801. Origination Fee: These are lender fees to cover the administrative costs in processing the loan. They are often expressed as a percentage of the loan and can vary among lenders.
802. Loan Discount: Points or discount points are a one-time fee by the lender or broker to pay for a particular interest rate. Each "point" is equal to one percent of the mortgage amount.

Other Items Payable in Connection with the Loan: These are fees that the lender charges to process, approve and make the mortgage loan.

Series 800 fees are guaranteed for 30 days from date this document is signed.			Paid by Borrower
801. Loan Origination Fee	%	to:	$
802. Loan Discount	%	to:	$
803. Appraisal Fee		to:	$
804. Credit Report		to:	$
805. Lender's Inspection Fee			$
806. Mortgage Insurance Application Fee		to:	$
807. Assumption Fee			$
808. Flood Certification Fee		to:	$
809. Mortgage Broker Fee	%	to:	$
810. Tax Service Fee		to:	$
811. Processing Fee		to:	$
812. Underwriting Fee		to:	$
813. Wire Transfer Fee		to:	$
814.			$

900. Items Required By Lender To Be Paid In Advance: Interest here is assessed from the date of closing to the end of the month. If no date has been set at the time of issuance of this document, an estimate is provided. The actual amount at closing will be the amount of days remaining in the month times the daily rate of interest based upon the rate of the mortgage. Premiums (lines 902-904) represent advance payment for required insurance.

Series 900 Fees are only estimates. If amounts change, a revised document will be issued.				Paid by Borrower
901. Interest from ___________	to _____________	@$	/day	$
902. Mortgage Insurance Premium for	_____________	months to	_____________	$
903. Hazard Insurance Premium for	_____________	months to	_____________	$
904. Flood Insurance Premium for	_____________	months to	_____________	$
905. VA Funding Fee				$

1000. Reserves Deposited With Lender (Escrow Account Deposits): These fees identify the payment of taxes and/or insurance and other items that must be made at settlement to set up an escrow account. The lender is restricted in the amount that can be collected. The individual item deposits may overstate the amount that can be collected.

Series 1000 Fees are only estimates. If amounts change, a revised document will be issued.			Paid by Borrower
1001. Hazard insurance	_____________ months	@$ _____________ per month	$
1002. Mortgage insurance	_____________ months	@$ _____________ per month	$
1003. City property taxes	_____________ months	@$ _____________ per month	$
1004. County property taxes	_____________ months	@$ _____________ per month	$
1005. Annual assessments	_____________ months	@$ _____________ per month	$
1006.	_____________ months	@$ _____________ per month	$
1007.	_____________ months	@$ _____________ per month	$
1008.	_____________ months	@$ _____________ per month	$

Guaranteed Good Faith Estimate (Discussion Draft)

Continued (Page 2)

1100. **Title Charges**. The following fees are not charged by your lender, but by the title company and/or other providers of title-related services you decide to use. The services identified are either required in connection with the loan or can be expected in your transaction. The estimates shown are based on:

the lender's experience in the community where the property is located, or

estimates provided by [Name of Title Company], a company [ ] affiliated
[ ] not affiliated with the lender.

You are free to shop for these services and are not required to use any particular title company.

Series 1100 Fees are only estimates.		Paid by Borrower
1101. Settlement or closing fee	to:	$
1102. Abstract or title search fee	to:	$
1103. Title examination fee	to:	$
1104. Title insurance binder	to:	$
1105. Document preparation fee	to:	$
1106. Notary fees	to:	$
1107. Attorney's fees	to:	$
1108. Title insurance binder	to:	$
1109. Lender's coverage	$	$
1110. Owner's coverage	$	$
1111. Commitment fee	to:	$
1112. Endorsement fee	to:	$
1113. Wire fee	to:	$
1114. Electronic doc. Fee	to	$

1200. Government Recording and Transfer Charges: These fees may be paid by you or by the seller, depending upon your agreement of sale with the seller. The buyer usually pays the fees for legally recording the new deed and mortgage (line 1201). Transfer taxes, which in some localities are collected whenever property changes hands or a mortgage loan is made can be quite large and are set by state and/or local governments. City, county and/or state tax stamps may have to be purchased as well (lines 1202 and 1203).

Series 1200 Fees are only estimates. If amounts change, a revised document will be issued.				Paid by Borrower
1201. Recording fees:	Deed $	; Mortgage $	; Releases $	$
1202. City/county tax/stamps:	Deed $	; Mortgage $		$
1203. State tax/stamps:	Deed $	; Mortgage $		$
1204.				$
1205.				$

1300. Additional Settlement Charges:		
1301. Survey	to	$
1302. Pest inspection to	to:	$
1303. Home Warranty Fees	to:	$
1304. Elevation Certificate	to:	$
1305.		$
	Total Costs to Close this Transaction:	$

Loan Officer **Date**

Applicant **Date** **Applicant** **Date**

RESPA Comment Letters

Selected Excerpts from Government Agencies

Board of Governors of the Federal Reserve Staff Comments (June 13, 2008)

- Board staff believes that the agencies should continue to pursue ways to harmonize TILA and RESPA consistent with the Congressional mandate. (page 2)
- HUD's proposal, however, departs from the approach of a single, integrated disclosure form with little rationale. (page 2)
- We believe that the inconsistencies and other differences between the proposed GFE and TILA disclosure are likely to confuse consumers and, undermine consumers' ability to make informed shopping decisions and avoid unnecessarily high settlement costs. (page 4)
- It does not appear that HUD's testing focused on how consumers understood the specific terms being disclosed on the revised GFE or whether they understood the multiplicity of terms represented in the different loan choices in the side-by-side comparison. (page 4)
- Additional work is needed to test and develop a better disclosure. (page 5)

Federal Deposit Insurance Corporation (undated)

- We have concerns about the length of the proposed GFE and the fact that it does not contain important information about certain loan costs. (page 1)
- We are concerned about whether the proposed GFE truly provides information that consumers need in an easily understandable format. (page 2)
- Additional information often makes a form less useful because the basic concepts are overlooked, and that items of interest to policy experts often do not convey information that consumers use. (page 2)
- At four pages, the proposed GFE may be too long and provide too much information for it to be understood and appropriately used by consumers. (page 2)
- We are not aware of an appropriate means of evaluating whether overall consumer costs would decline as a result of average cost pricing. (page 4)

FTC and Bureau of Consumer Protection Staff Comments (June 11, 2008)

- FTC staff supports the development of a single mortgage disclosure document, rather than separate disclosures under RESPA and TILA, so that consumers shopping for a mortgage loan would not need to consult several different disclosure documents to obtain a fuller picture of the loan terms. (page 3)
- The staff recommends that HUD collaborate with the Board of governors of the Federal Reserve System (Federal Reserve Board) to consolidate and reform federal mortgage disclosures. (page 3)
- [P]roposals may have the unintended consequences of further complicating the already complex mortgage lending process, thus causing more consumer confusion than clarity. (page 3)
- FTC staff encourages HUD to consider whether pricing restrictions on the re-sale of settlement service components and prohibitions on referral fees may inadvertently decrease competition and efficiency in the settlement service market. (page 5)

Small Business Administration Office of Advocacy (June 11, 2008)

- Advocacy is concerned that HUD may have underestimated the costs of the proposal and created a potential uneven playing field for some small entities. Moreover, there may be less costly alternatives that achieve HUD's stated goals. (page 2)
- Advocacy urges HUD to give full consideration to the economic information and alternatives suggested by small entities prior to going forward with the final rule. (page 6)
- We respectfully advise HUD to document the additional costs to small entities and consider harmonizing the GFE with the HUD-1 as well as clarifying the provision on tolerances. (page 6)
- Office of Advocacy supports HUD moving forward without the closing script requirement, the volume discount language, and the YSP classification. (page 6)

The Estimated Costs of HUD's Proposed RESPA Regulations

Prepared for the National Association of Realtors®

By

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HUD issued a revised set of RESPA regulations on March 14, 2008, following nearly six years of review. These new regulations attempt to improve upon an earlier HUD proposal, issued in 2002 and subsequently withdrawn due to strong opposition. As before, the primary objectives of HUD's proposal are to promote shopping, bring greater "certainty" to closing costs, and simplify and improve the mortgage origination process. However, while these goals are laudable—and while the Department seems to be moving in the right direction—the new proposal still falls short on many of its stated objectives.

There are numerous operational and legal issues that are associated with the proposed regulations. However, this paper focuses on the regulatory impact analysis (RIA) that is used to justify HUD's proposal, in particular, on its estimates of compliance costs. While the RIA is voluminous and covers a variety of topics, HUD's analysis ultimately comes down to a set of relatively simple calculations that attempt to quantify the relative costs of two key aspects of the proposal:

- the revised Good Faith Estimate (GFE); and
- the addition of a "Closing Script" to the settlement process.

This paper discusses some of the limitations of HUD's analysis, and the sensitivity of its estimates to alternative assumptions regarding the probable outcome of the new regulations.

1.0 Key Aspects of the New RESPA Requirements

By HUD's own admission, its new RESPA requirements will fundamentally change the mortgage industry's business model. The redefined GFE and the inclusion of a closing script will add new procedures and risks to both the loan origination and closing process.

The new GFE will be standardized, have a summary page that captures the major elements of origination and closing costs, and contain three additional pages designed to help consumers evaluate the relative attractiveness of a loan. Among other things, these additional pages will provide a more detailed breakdown of closing costs, as well as a chart presenting alternatives offering higher (and lower) interest rates coupled with correspondingly lower (and higher) up-front costs. In redesigning the GFE, HUD has attempted to give consumers the information that they need to shop for loans and evaluate and compare the different offers they receive.

However, the potential impact of HUD's new regulations extends well beyond the format change embodied in the revised GFE. To begin with, the GFE is currently issued after a borrower has applied for a loan. Under the new regulations, a GFE would be required *prior* to loan application. As noted by HUD, these new regulations will effectively create two types of applications: one for the GFE, another for the actual mortgage. The reason for this new requirement is straightforward: HUD wants consumers to use the GFE to facilitate their shopping process. Presumably, if the regulations have their intended effect, the "typical" consumer would obtain two or more GFEs before actually applying for a loan.

In addition, when a GFE is issued, the originator (defined as the lender or the mortgage broker) will now be required to guarantee the origination fee and certain third party closing costs (e.g., title insurance, appraisal, etc.) for a minimum of 10 business days (subject to certain tolerance levels.) The originator must also specify an interest rate and a lock-in period for the rate, although the originator is free to choose the length of the lock-in period. Once the borrower has accepted the offer and locked-in the interest rate, the terms identified on the GFE would generally be guaranteed until the loan is closed. While HUD has allowed for some discrepancies in the event of "unforeseen circumstances" (e.g., Acts of God, need for a second appraisal, etc.), changes resulting from movements in interest rates or other economic developments are specifically not allowed.

HUD acknowledges that certain information on the borrower will be required in order to guarantee the GFE. As a result, the new regulations will allow the loan originator to collect basic information on the applicant (i.e., name, social security number, property address, estimated value of the property, and loan amount) before issuing a GFE. If a preliminary review of the data suggests that the borrower would not be qualified for the requested loan, the originator can either reject the application or issue a new GFE for an alternative product. In either event, the originator must keep a record that documents why the decision was made.

Thus, the new GFE requirement will effectively create two distinctly different underwriting processes corresponding to each application type: an initial underwrite for any consumer who requests a GFE based on the limited data provided in the GFE application (i.e., credit score, stated income, loan amount, and estimated property value or sales price); and a second, more comprehensive underwrite for the subset of consumers who ultimately apply for the loan based on more extensive information collected and validated as part of the traditional underwriting process. If consumers use the GFE as a shopping tool, loan originators will have to conduct initial underwrites on large numbers of consumers who end up going elsewhere or not getting a mortgage at all.

Finally, to help ensure that consumers understand the terms of their mortgages and that closing costs do not exceed the thresholds identified in the GFE, HUD has added a new "closing script" to be read to the borrower at the settlement table. The script would contain detailed information about the terms and conditions of the mortgage. It would also include a chart that compares the "firm" costs contained in the GFE to their corresponding line items in the HUD-1 form. While HUD believes that such a comparison will prevent instances of "bait and switch", the Department does not establish a process for resolving any discrepancies that are uncovered at closing, or to otherwise enforce the "guaranteed" nature of the GFE.

2.0 The Potential Impact of HUD's Proposal

As noted earlier, HUD's Regulatory Impact Analysis is voluminous. An extensive review of the document would be impractical within the designated comment period (and probably not particularly productive.) However, a closer look at some of the assumptions that underlie the Department's estimates suggests that HUD has greatly underestimated the costs of the implementing its new requirements.

The Department estimates that revised RESPA regulations would save the average consumer about $660 in up-front loan origination and closing fees by facilitating and improving the shopping process. It also estimates that the annual compliance cost of producing these savings would be about $100 per loan—$45 for the revised GFE and another $54 for the closing script. Finally, HUD estimates that its proposal would produce efficiency gains of about $86 per loan for borrowers and about $112 per loan for originators due to a reduction in total time spent shopping (or dealing with shoppers.)"[1]

As described in more detail below, there are a number of reasons to suspect that HUD has significantly under-estimated the cost of implementation. In the end, more realistic assumptions concerning these costs would significantly reduce net savings to consumers.

2.1 Impact on Industry Structure

By HUD's own admission, the new RESPA requirements would fundamentally change the mortgage origination process. However, HUD's analysis completely ignores the proposal's potential impact on the structure of the industry. This "partial equilibrium" approach brings the Department's estimates of costs and benefits into question.

Under HUD's proposal, loan originators (and mortgage brokers) will be asked to guarantee not only their own fees, but the fees of third-party settlement service providers. To manage the resulting risk, originators will inevitably seek out contractual arrangements (and pricing concessions) with one or more service providers. As originators seek to form these arrangements, there will be clear winners and losers

[1]HUD estimates that the average consumer would save about an hour in time spent shopping for a mortgage and settlement service providers. It also asserts that these time savings would be realized by originators and settlement service providers since these entities would spend less time answering questions and "seeking out vulnerable borrowers." However, HUD offers no real justification for these estimates. See US Department of Housing and Urban Development, "RESPA: Regulatory Impact Analysis and Initial Regulatory Flexibility Analysis FR-5180-P-01. Proposed Rule to Improve the Process of Obtaining Mortgages and Reducing Consumer Costs," Office of Policy Development and Research. P. 3-120.

throughout the mortgage and settlement services industries. While HUD seems to imply that the only losers will be inefficient or unscrupulous service providers, most commentators believe that, for a variety of reasons, small originators, brokers and settlement service providers will lose at the expense of larger entities.

For example, if the originator requires the borrower to use one of its own service providers, it would probably want to limit its agreements to firms that can handle relatively a large number of transactions. Smaller service providers, who are more likely to have capacity constraints, would inevitably be disadvantaged. Why would a loan originator choose to identify, negotiate, monitor and track the rates of 15 or 20 smaller companies when the same volume of loans could be handled by one or two larger firms? Even if the originator does not require the borrower to use one of its own service providers, it must provide a list of "acceptable" providers as part of the GFE. Since the originator will still be required to guarantee the rates of these recommended companies, such lists are also likely to be short.

The proposed regulations will also tend to favor larger lenders and brokers. Larger originators are in a better position to negotiate rates and to extract pricing concessions from third party settlement service providers. While this may be good for consumers in the short-term, the increased concentration that would inevitably result could eventually produce the opposite effect. For example, larger originators may use their market power to undercut their competitors, and then subsequently move to higher rates once their competitors have left the market. Regardless of the eventual impact, the number of active players in the market would undoubtedly decline.

While the Department admits that "a new business model is being put in place for the mortgage industry," it makes no attempt to take these secondary effects into account in estimating the costs and benefits of the proposal. In fact, HUD dismisses the issue by stating that "it is difficult to provide comments on a market structure that does not yet exist."[2] Given the current turmoil in the mortgage market, one wonders if now is the time

[2] HUD, op. cit. p. 3-87.

to implement a new regulation that would result in such structural change. At a minimum, this issue deserves to be given more than cursory attention from HUD before it finalizes its regulation.

2.2 The Cost of the New GFE

The Department also underestimates the costs of implementing the new GFE requirements. Among other things, HUD's proposed regulations will require the industry to modify its existing software programs, train staff on the use of the form, process and track multiple applications from multiple borrowers, underwrite GFE applications for borrowers who end up going to other lenders, and require originators to assume the additional risks and costs that are associated with the mandated tolerance levels on the GFE.

HUD estimates that the annual cost of the expanded GFE will be $44.50 per loan. However, in deriving its estimates, HUD either ignores or dismisses many of the factors noted above. This section highlights some of the major limitations of HUD's analysis, which include:

- understating the total number of GFEs that would need to be issued and tracked;
- ignoring the operational and hedging costs associated with the guarantee; and
- ignoring the costs of the initial underwrite, including the costs of obtaining additional FICO scores.

Accounting for these and other factors would significantly increase the estimated costs of the GFE.

The Number of Good Faith Estimates

HUD assumes that roughly 1.7 GFEs would be produced for every completed mortgage origination. Thus, in order to produce 12.5 million loans (HUD's baseline estimate for a typical year), HUD assumes that originators would have to issue roughly 21.250 million GFEs (i.e., 1.7 GFEs per loan x 12.5 million loans.) The 1.7 ratio used by HUD is based on the observed relationship between loan applications and loan originations, as reported in HMDA data.[3] (The ratio is significantly higher than 1.0 due to the fallout that occurs when loan applications are either rejected or voluntarily withdrawn.) In effect, using a 1.7 ratio to estimate the number of GFEs that are associated with a given origination volume assumes that the new regulations will not affect the total number of GFEs that are issued in any given year (or, alternatively, that there will be just one GFE per mortgage application.)

However, there are a number of reasons that a higher ratio should be used. Assume, for example, that the revised GFE does not affect the fallout that occurs once a formal application has been received (i.e., that the ratio of mortgage applications to originations remains at 1.7.) Even if the average borrower obtained just two GFEs, the total number of GFEs in a typical year would rise from 21.3 million (HUD's estimate) to about 42.5 million (i.e., 2 GFEs per application x 1.7 applications per loan x 12.5 million loans.) While one could argue that better information on the part of consumers would reduce the number of loans that were rejected or withdrawn after a loan application has been filed, even if the fallout rate were cut in half—a highly unlikely event—the number of GFEs that are issued in a typical year would be 33.75 million, or about 59 percent higher than the estimate used by HUD.[4]

Thus, it seems highly likely that the ratio of GFEs to loan originations that is embedded in HUD's projections (1.7) is far too low. Under the alternative assumptions presented above, the ratio of GFEs to originated loans would more likely range between 2.7 and 3.4 even if one assumes that the average consumers obtains just two GFEs. These higher ratios would translate into proportionally higher compliance costs.

[3] HUD, op. cit., p. 2-6.

[4] Cutting the fallout rate by half would result in a ratio of 1.35 loan applications for each originated loan. Assuming that each borrower obtains 2 GFEs before a applying for a loan—and that it there are 1.35 applications for every loan—results in 2.7 GSEs per origination.

In deriving its estimates, HUD assumes that the annual costs of the revised GFE primarily relate to processing and tracking the applications.[5] If one assumes that 21.250 million GFEs would be issued in a typical year, average costs per originated loan would be $44.50—the estimate produced by HUD. However, if one assumes that between 34 and 43 million GFEs would be issued, the average annual cost per originated loan would rise to $71 to $89, respectively.

While the ratios that are used to derive these various estimates are admittedly somewhat arbitrary, one thing seems clear: either HUD has seriously under-estimated the number of GFEs that will be issued under its new regulations or the regulations will not produce the amount of shopping behavior that the Department would like to achieve.

The Operational and Hedging Costs of the GFE

As noted above, HUD's estimates of the on-going costs of the GFE are primarily based on the amount of additional time it will take to process the application and produce the revised GFE form. HUD ignores or dismisses the operational and hedging costs that would be associated with this new requirement, including the costs of hedging the interest rate that is offered on the GFE.

Under the proposed regulations, the originator's fee (excluding the YSP) and certain components of closing costs must be guaranteed for at least 10 business days (subject to a 10 percent tolerance level that is applied to the sum of all applicable third-party costs.) However, HUD allows the originator to establish the lock-in period for the interest rate. Until the rate is locked, all interest-related charges, including the yield spread premium, are allowed to float.

Conceivably, the originator could choose a lock-in period that is considerably shorter than the 10 business days required for other components of the GFE in order to minimize

[5] As described in more detail below, HUD either ignores or dismisses the additional underwriting, operational and hedging cost that would be associated with the new guarantees.

its hedging costs. While this would defeat one of the major objectives of HUD's proposal—namely, to fix the mortgage terms for at least 10 business days in order to facilitate the shopping process—HUD does not address this issue in its RIA. Instead, HUD asserts that its decision to reduce the guarantee period from 30 to 10 business days would eliminate any significant operational and hedging costs that were associated with its 2002 proposal.

However, even a relatively short lock-in period for the interest rate on the GFE could add significant costs to the originator over and above the hedging costs that now occur once a formal application has been received. Suppose, for example, that originator set the lock-in period to 10 business days—a move that would certainly make the offer much easier for consumers to understand and would be consistent with HUD's objectives.[6] According to our estimates, the cost of the hedge would be about 4 basis points (i.e., 0.04 percent) of the dollar value of requested loan.[7] If one assumes that 3.7 GFEs are issued for every loan that gets originated, the initial interest lock would cost about 13.6 basis points per loan (i.e., 4 bps per GFE x 3.7 GFEs per origination.) On a $200,000 mortgage, this would add about $272 to the cost of the loan. Even if one uses HUD's assumptions regarding the ratio of GFEs to originations, the average cost of the interest rate hedge would be about $180 per loan (i.e., 4 bps per GFE x 1.7 GFEs per origination.)

Multiple Underwriting

HUD has also not factored in the additional costs of underwriting the GFE. While it notes in its RIA that the originator would be required to update the credit report once a formal loan application has been received[8], it makes no attempt to account for this

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[6] HUD's revised GFE has multiple dates for the offer: one for the origination fee and third party settlement costs; one for the quoted interest rate; one for the settlement date; and one for the number of days that the loan must lock before closing. The multiplicity of dates could well lead to borrower confusion.

[7] The value of the hedge can be estimated by comparing differences in the rates that Fannie Mae and Freddie Mac are currently being offering for loans with different delivery periods. On May 15th, the interest rate spreads on Fannie Mae and Freddie Mac 30 and 60 day deliveries were about 8 basis points. Guaranteeing the interest offered on the GFE for 10 business days (i.e., 12 to 14 calendar days) would cost about half of this amount, or roughly 4 bps.

[8] HUD, op. cit. p. 3-70.

additional step in its cost analysis. In effect, HUD assumes that the initial screening that would occur when the GFE is issued would simply replace the initial screening that would otherwise occur once a formal application has been received. This argument might make some sense if one accepts HUD's premise that its new regulations will not affect the number of GFEs that are ultimately issued. However, the argument falls apart if one assumes that HUD's regulations will lead to significant increases in the total number of GFEs.

For example, if one assumes that the ratio of GFEs to originations is 2.7 instead of 1.7, loan originators would have to pull at least one additional credit report for every mortgage origination (i.e., 2.7 – 1.7). According to HUD, the average credit report costs about $25.[9] This additional expense would increase the Department's estimated cost of the GFE ($45 per loan) by 56 percent. Furthermore, the additional underwriting step would undoubtedly add to total processing time. If one assumes that preliminary screening will take about 10 minutes to complete, the total cost of the initial underwrite would rise to about $30 per loan—$25 for the initial credit pull and another $5 for the underwriter's time (valued at $31.14 per hour.)[10] If one assumes that the ratio of GFEs to originations is even higher—for example, 3.4—the additional underwriting costs would add about $52 to the cost of a typical loan.

Alternative Estimates of Annual Costs of GFE

Exhibit 1 summarizes how changes in HUD's assumptions could change the estimated cost of the GFE. The columns reflect different assumptions regarding the ratio of GFE applications to loan originations, which affect the number of GFEs that would be issued in a typical year. The first column assumes that the new regulations do not affect the total number of GFEs that are issued (i.e., HUD's assumption) and that the ratio of GFEs to total loans is 1.7. The second and third columns present alternative estimates based on

[9] HUD, op. cit. p. 3-95.
[10] HUD uses different hourly wages to value the originator's time. In its estimates of efficiency gains, HUD values the time saved by originators at $72 per hour. However, in its estimates of GFE costs, it uses $31.14 per hour. To be conservative, we use the lower figure here.

ratios of 2.7 and 3.4, respectively.[11] As described in an earlier section, such higher ratios are not unreasonable, particularly if consumers actually use the GFE to assist them in their shopping process.

Exhibit 1: Estimated Annual Cost of the GSE per Loan

	Number of GFEs Per Originated Loan		
	1.7	**2.7**	**3.4**
Processing Costs	$ 45	$ 71	$ 89
Hedging Costs[12]	$136	$216	$272
Initial Underwrite[13]	0	$ 30	$ 52
Added Cost per Loan	$181	$317	$413

As illustrated by the chart, accounting for hedging and underwriting costs, and applying more realistic assumptions regarding the expected number of GFEs, would have a dramatic impact on the estimated costs of the GFE. Instead of the $45 estimated by HUD—the number presented in the upper left hand cell of the chart—projected costs could easily range from about $300 to $400 a loan. Moreover, even these higher estimates may be conservative. For example, they do not include any legal costs associated with the litigation risk that would inevitably arise from a "guaranteed" GFE.

[11]The 2.7 ratio assumes that the average consumer obtains 2 GFEs and that the fallout rate from application to origination is reduced by half (i.e., to 1.35). The 3.4 ratio assumes that the average consumer obtains 2 GFEs and that the ratio of applications to originations remains the same (i.e., 1.7).

[12] Assumes that the interest rate offered on the GFE is good for 10 business days and that the average loan amount is $200,000.

[13]The estimates assume that an applicant's credit report is pulled only once, when the GFE is approved. This may be unrealistic given the time that could elapse between GFE and loan application. Costs would be higher if one assumes that credit scores would have to be pulled again when the borrower actually applies for a loan.

2.0 The Costs of the Closing Script

HUD also underestimates the cost of the proposed closing script, which would provide little, if any value to the consumer. By the time the consumer comes to closing, it is far too late to change the terms of the loan. And if discrepancies in closing costs are found, there is no established process to resolve such issues or to enforce the guarantees established by the GFE.

Implementation issues aside, HUD assumes that preparing and delivering the closing script will take about 45 minutes of the closing agent's time, which would double the amount of time typically required to close a loan. HUD estimates that this additional step would add about $54 to the cost of the loan, or about $1.20 for each additional minute that the title agent spends in preparing and delivering the closing statement.

While HUD calculates the cost of this requirement on the settlement agent's part, it either dismisses or ignores the costs to the other participants at the closing table, including the borrower, the borrower's spouse, the real estate agent, and in some states, two or three attorneys. HUD claims that its requirement will impose no additional costs on borrowers, since they would otherwise be left on their own to review and compare the GFE to the fees recorded on the HUD-1 form. However, even if one accepts this premise, there are likely to be additional professionals at the closing table who will have to sit through a longer settlement process.

HUD estimates that it will take about 15 minutes to read the closing script and answer any questions. Assuming that the opportunity costs for everyone present would be about the same as the closing agent's time, the cost of the closing script would rise by about $18 for each additional person involved. For example, if one assumes that three additional people are present at closing, the cost of the closing script would double to $108—$54 for the closing agent's time (45 minutes) and another $54 for the time of the three other attendees combined (3 x 15 minutes, or 45 minutes.)

HUD also fails to recognize the impact that increasing the amount of time at closing would have on other related costs. Most closings occur at or near the end of the month. Roughly doubling the amount of time that it would take to complete the transaction would create additional demands on space to handle the same volume of loans. Yet such additional costs are not considered in the Department's analysis. Nor does the Department consider the legal and regulatory risk that now must be borne by the closing agent. In effect, HUD's proposal would have the closing agent act as the consumer's representative and serve as the "RESPA police." Aside from legal questions regarding whether closing agents other than attorneys can play such a role, the requirement would expose the closing agent to additional legal and regulatory risk, which would once again increase the costs of closing.

The Department also fails to document the benefits that flow from the closing script. By the time the borrower reaches the closing table, it is highly unlikely that he or she will walk away the transaction unless serious misrepresentations or issues are uncovered. For example, according to the Department's estimates, typical charges for title services and other third party fees come to about $1841.[14] Thus, a variance of greater than $184 would cause a potential RESPA violation. Indeed, in two of the examples presented in the Federal Register, differences of $14 to $15 could potentially bring the closing process to a halt.[15] It is highly unlikely that anyone involved in the settlement process would walk away at this point in the process. Someone—either the closing agent or the real estate agent—would undoubtedly reach into their pockets to pay for an excess that was the responsibility of the loan originator.

While HUD has allowed for fees that exceed the tolerance level to be justified and resolved at the closing table, the most likely party to resolve any discrepancies—the loan originator—would typically not be present. If the lender were required to be available by

[14]According to the Urban Institute, total title fees and other third party charges had medians of $1267 and $574, respectively. See Federal Register, Vol. 73, No. 51, March 14, 2008, p. 14106.

[15] In one example, the GFE estimated third party closing costs at $642, while actual costs came in at $715. The difference ($78) exceeded the 10 percent tolerance level by $14 (i.e., $78 - $64.) See Federal Register, op. cit., p. 14079. In another example, third party costs were estimated to be $809, but came in at $905. The difference ($96) exceeded the 10 percent tolerance level by $15 (i.e., $96 - $81.) See Federal Register, op. cit., p. 14091.

phone at the time that the script were read, this would add another $18 to the estimated cost of this provision (assuming that the value of the originator's time was the same as the closing agent's.)

In short, HUD estimates that the closing script would add about $54 to the average cost of a loan. However, more reasonable assumptions would yield costs that are probably at least double this amount.

4.0 Impact on Shopping

The Department states that it "hopes" that the four page GFE form—along with its accompanying guarantees—will be delivered to consumers free of charge. However, even if this occurs, lenders will undoubtedly seek to recoup their additional costs as part of the origination fee. This was the assumption used by HUD in deriving the estimated costs of its proposal; it was also used to derive the alternative estimates presented here.

If, on the other hand, lenders decide to charge for the form, the GFE could actually *decrease* the amount of shopping that occurs—thereby negating the very benefits that the Department is attempting to achieve. Even if one accepts the Department's estimate that the cost of the GFE would be just $45, charging the consumer this amount simply to provide a quote would put a significant damper on the amount of shopping that actually occurs.

5.0 Conclusions

HUD estimates that the on-going costs of its new regulations would be about $100 per loan—$45 for the revised GFE and $54 for the closing script. However, the analysis presented here shows that actual costs are likely to be considerably higher. Even under reasonably conservative assumptions, the average cost of the GFE would be well over $300 per loan, while the cost of the closing script would probably be closer to $100. As a result, a relatively large share of the savings that are envisioned by the Department could easily be absorbed by these higher costs.

It is important to recognize that most of the additional costs described in this report are associated with the guarantee embedded in the revised GFE, as opposed to the form *per se.* The Department should seriously question whether its desire to provide greater certainty in closing costs is worth these additional costs. Presumably, a simplified GFE could produce many of the shopping benefits envisioned by HUD by making the terms of the loan more transparent.

Indeed, an earlier study by HUD concluded that on average, closing costs on the GFE were relatively good predictors of closing costs and were, in fact, slightly higher than those recorded on HUD-1 forms.[16] While the study was based on a small number of observations—and while it found that actual closing costs were significantly higher than those provided by the GFE in an unspecified "minority" of cases—the Department has offered no compelling evidence that "bait and switch" is a widespread phenomenon.

Presumably, HUD could achieve most, if not all of its stated objectives by simplifying and standardizing the GFE without imposing additional costs, complexities and paperwork on a process that is already far too cumbersome. In the end, the simplest solution may be the one most likely to succeed.

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[16] Mark Shroder, "The Value of the Sunshine Cure: The Efficacy of the Real Estate Procedures Act Disclosure Strategy," Cityscape: A Journal of Policy Development and Research, Vol. 9, Number 1, 2007.