

# Maryland Association of Mortgage Brokers Continuing Education Forum

RESPA Compliance  
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## RESPA Overview

Three major developments have led to standardization of residential real estate transactions:

1. the emergence of federal (and to some degree state) programs to insure or guarantee residential mortgage loans;
2. the increasing dominance of residential mortgage lending practices, procedures, and documentation by the secondary purchasers of residential mortgage loans, and
3. the passage in 1974 of RESPA.



# RESPA Overview

- Real Estate Settlement Procedures Act of 1974--RESPA
- Implemented by HUD Via Its Regulation X (24 CFR § 3500 *et seq.*)
- Primary purposes: 1) disclosure to the consumer of the nature and costs of the settlement process, and 2) the curtailment of abusive practices by settlement service providers through prohibition of compensated referrals and kickbacks, splits of fees, and unearned fees. In conjunction with TILA, RESPA was intended to give a borrower a framework for understanding residential loan transactions.
- Contains Civil and Criminal Provisions
- Procedural and Substantive Provisions



## RESPA Applicability


RESPA Regulates the Settlement Process  
for Federally Related Mortgage Loans  
including “settlement services”:

- What is “Settlement”?
- What is a “Federally Related Mortgage Loan”?




# RESPA Applicability

- “Settlement Service” Means any Service Provided in Connection With a Prospective or Actual Settlement.
- Includes: the Origination of a Federally Related Mortgage Loan
  - Taking of Loan Applications
  - Loan Processing
  - Underwriting and Funding of Such Loans
- Mortgage Brokerage
- Provision of Any Services Related to the Origination, Processing, or Funding of a Mortgage Loan




# Procedural and Substantive Requirements—RESPA Requires:

- Estimated and Actual Settlement Costs
  - Good Faith Estimate – 3 days after application
  - “Required Providers”
    - Must state that use of provider required and estimate is based on charges of the provider
    - Must give name, address, and telephone number of each provider
    - Describe the relationship between each such provider and the lender



# Procedural and Substantive Requirements—RESPA Requires:

- HUD-1 or HUD-1A
  - Is the Closing Statement “Accounting Sheet”



# Procedural and Substantive Requirements—RESPA Requires:

- Escrow Accounting
  - Initial and Annual Statements
  - Limit on “cushion” amounts
- Mortgage Servicing Notices
  - Initial disclosure at application whether the servicing is likely to be transferred
- Mortgage Servicing Transfers
  - Hello/Goodbye Letter



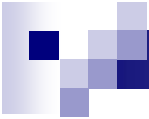
# Sections 8(a) and 8(b) of RESPA

- Section 8(a) Prohibits Direct or Indirect Kickbacks and Referral Fees
- Section 8(b) Prohibits Excessive Payments, Unearned Fees, Fee Splitting and Similar Payments



# Section 8(a) – Dirty Kickbacks

- Fax Machines
- Tickets to Basketball Games
- Naked Bribes
- Free Office Space or Payment of Overhead
- Lottery Tickets
- (HUD Never Saw a Payment That Was Not a Kickback)



Important Caveat!!!! Section 8(c)  
of RESPA Contains Exceptions

“Nothing in This Section Shall Be Construed  
As Prohibiting...the Payment to Any  
Person of a Bona Fide Salary or  
Compensation or Other Payment for  
Goods or Facilities Actually Furnished or  
for Services Actually Performed....”



# Another Limited Exemption for Referrals to Affiliates

## ■ Affiliated Business Arrangements

- When referring business to an affiliate or 1% owned company
- Give disclosure of ownership arrangement (AfBA disclosure) and estimate of costs of referred business
- Exemption from Section 8 only for “dividends” and other returns on ownership, not for other payments



# Broker Policy Statement

- HUD Adopted a List of Services That May Be Performed by a Broker In Exchange for a Fee
- Taking the Application\* Plus 13 Other Loan Origination Activities
- A Broker Must Take the Application Plus At Least 5 Others
- Counseling Versus Non-Counseling Functions
- A Reasonable Fee May Be Paid



# **“Yield spread premiums” under RESPA**

- **YSP is money paid to the broker for delivering higher rate loan**
- **YSP also is convenient way for borrower to pay broker fee through rate instead of cash at closing**
- **Hundreds of class actions brought against industry**
- **HUD finally settled issue stating “all broker compensation from all sources must be measured against all services performed by the broker”**
  - **Key: Case by case analysis required – no class action**



# Recent HUD Action

## HUD Inspector General Found “Quality Program” Violates RESPA

- On July 14, HUD concluded that First Magnus Financial Corporation violated RESPA when it actually paid brokers volume-based incentives.
- Incentives deemed inducements associated with the referrals of brokered FHA mortgages and not related to quality.

HUD is watching Broker Compensation under Quality Control Programs for any compensation related to volume.



# HUD Letter-Brokering FHA Loans

## HUD Reminds Lenders of FHA Rules for Dealing with Mortgage Brokers

- On June 20, a mortgagee letter reminded lenders of various payment and service restrictions when dealing with non-FHA-approved mortgage brokers for forward mortgages.
- The letter makes clear that, although a borrower may engage a non-FHA-approved mortgage broker for counseling services, loan origination services may not be performed by the broker and the FHA-approved mortgagee may not compensate the broker for the counseling services.
- To the extent a borrower receives counseling from a non-FHA-approved mortgage broker, the services must constitute “meaningful counseling” and the fees must be paid from the borrower’s own available assets and disclosed on the HUD-1.
- \*HERA eliminated participation in the HECM Advisor Program by non-FHA approved counselors.



# Proposed RESPA Reform Rule - Status

- August 7, 2008--letter to HUD, signed by over 240 Members of Congress urging withdrawal of the proposed RESPA rule.
  - Requested joint rulemaking with the Federal Reserve Board.
- After Labor Day--Another letter with approximately 30 more signatures sent to HUD.
- HUD sent final rule to OMB.
- HUD Secretary predicts rule will be finalized in December 2008 with an implementation date in January 2010.



# Themes of Proposal

- Enable consumers to obtain multiple GFEs to shop
  - At minimal cost and a minimal application process
- GFE includes very detailed loan terms and costs
  - No APR, but interest rate and monthly payment required
  - Particular detail on ARM loan adjustments
- Settlement costs are grouped in categories
- New accuracy requirements for GFE
- Closing script added to ensure consumer understanding of key terms and features
- Broker / Lender distinction blurred (YSP not shown)



# Initial Observations

- Rule impacts other laws (TILA, HMDA, ECOA)
- Greater disclosure means less simplicity
  - Will consumers read 4-page GFE?
  - Still have itemization
- Burden on lenders to pre-underwrite for nominal fee
- New notice requirements (counteroffer GFE or loan rejection notice in 1 day)
- Unclear authority for new tolerances and mandated GFE form
- Average Cost Pricing
- Elimination of “Required Provider” disclosure -helpful



# RESPA Reform Rule Highlights— Proposed GFE Application

Application Requires:

- Name and Social Security Number (to order credit)
- Property address
- Gross monthly income
- Borrower's information on the house price or best estimate of the property's value
- The amount of the loan sought

The GFE application may be taken orally but it must be reduced by the lender to a written or electronic record.



# New GFE Components: Loan terms

The new GFE is a 4-page document that provides a summary of loan terms and total settlement charges. Page 1 discloses:

- Initial loan amount
- Loan term
- Initial interest rate and the specific date it remains available
- Initial monthly payment owed for principal, interest and mortgage insurance (but not taxes)
- Rate lock period
- Whether the interest rate can rise, and the maximum
- Whether the loan balance can rise, and the maximum
- Whether the monthly payment (P,I, MI) can rise, and the maximum
- Whether the loan has a prepayment penalty, and the maximum
- Whether the loan has a balloon payment, and description
- Whether the loan has a monthly escrow payment for taxes and other obligations
- The specific date the estimate for settlement charges remains available



# New GFE Components: Settlement Charges

Page 1 of the new GFE also discloses a total amount for each of:

- A. Your Adjusted Origination Charges
- B. Your Charges for All Other Settlement Services
- A+B. Total Estimated Settlement Charges (which is the sum of A and B)

Page 2 of the GFE describes the components of these figures



# New GFE Components: Recasting Yield Spread Premiums.

- YSPs are not disclosed as “YSPs” on the GFE.
- All direct broker charges are included in “Our Service Charge”
- A YSP (the amount paid to the broker by the lender above the amount needed to fund the loan) is shown as a credit for the specific interest rate chosen –which reduces total origination charges
- Discount Points (a “charge”) collected by the broker to be paid to the lender would be netted against any YSP (“credit”) and shown as net “credit” or “charge” depending upon which is larger.
- A “Credit” and “Charge” cannot both be shown in the same transaction



# GFE Components: Your Charges For Other Settlement Services

Page 2 of the new GFE discloses other settlement charges in 8 separate categories, as follows:

- “Required services that we select” (other than title) (Block 3): price for each service, plus total(e.g. appraisal, credit report, etc.)
- Title services and lender’s title insurance (Block 4)
- Required services that you can shop for (other than title) (Block 5): estimated price for each service, plus total (e.g. attorney, closing services, notary). If the borrower is permitted to shop for required settlement services, the loan originator must provide a written list of settlement service providers at the time of the GFE on a separate sheet of paper.
- Government Recording and Transfer Charges (based upon proposed loan amount and property address) (Block 6)
- Reserves or escrow (for taxes and insurance) at settlement (Block 7)
- Daily interest charges (showing # of days until specific closing date) (Block 8)
- Homeowner’s insurance (premium at settlement) (Block 9)
- Optional owner’s title insurance (Block 10)

# GFE Tolerances

Page 3 of GFE highlights charges with restricted tolerances-- all other settlement charges may change

- Charges with **zero tolerance** (can't increase)
  - the loan originator's service charge,
  - the charge or credit for the specific interest rate chosen (while the rate is locked), and
  - government charges.
- Charges with **10% tolerance** (in aggregate):
  - lender-required and selected services, i.e., "Services we select" (appraisal, credit, etc.) and, if applicable, title
  - lender-required services (including lender's title insurance and optional owners title insurance), where the borrower selects the provider from a list supplied by the originator.

Above charges can also change if "**unforeseeable circumstances**"



# New GFE Loan Comparison Chart

- Page 3 of the new GFE provides a rate/cost “teeter-totter” chart showing the subject loan amount and rate requested compared with alternative loans with the same loan amount and terms, but not showing (i) a loan with a higher interest rate and lower settlement charges; and (ii) a loan with a lower interest rate and higher settlement charges.
- This chart must also show changes in the monthly payments for the loans. For ARM loans, the initial rate only may be shown.



# **New GFE – Additional Disclosures**

On page 4 of the new GFE, the originator must provide estimated annual amounts for:

- Property taxes,
- Homeowner's insurance,
- Flood insurance, and
- other required property protection insurance



# Fee Limit– Providing GFE

- HUD is concerned that under RESPA's current rules borrowers may pay significant fees before receiving a GFE, inhibiting shopping.
- Under the proposed rule, no fee may be charged as a condition of receiving the GFE except for the “cost of providing GFE,” including the cost of an initial credit report.



# Timing for GFE Terms Available

- Under the proposal, the GFE terms must be available for at least 10 business days from GFE delivery, except for:
  - charge or credit for the specific rate chosen
  - adjusted origination charges
  - per diem interest.



# Mortgage Application

- If the consumer chooses to pursue the GFE terms, then he or she would submit a “mortgage application.”
- “Mortgage application” includes all other information needed to underwrite the loan and/or to verify the information provided in the GFE application.



# Underwriting and Loan Denial Notices

- After final underwriting, the originator must notify a rejected borrower within 1 business day of the decision to reject.
- Where a borrower's GFE application is rejected, and another loan product is made available, the originator must provide the borrower with another GFE. The basis for the rejection or changes to the GFE must be documented and retained for at least 3 years after settlement.



# HUD – 1/1A/ Itemization

- Modifies the HUD-1/1A slightly to allow comparison of charges on the GFE.
- Basically, the HUD-1/1A lines would reference corresponding “Block” numbers on the GFE.



# No cost loans

- The disclosure of costs in a “no cost” loan is subject to complicated and somewhat confusing rules.
- Where “no cost” encompasses third party fees as well as the up-front payment to the loan originator (presumably by the lender), the third party services to be paid for out of the **adjusted origination charge** must be itemized and listed on the HUD-1/1A with the charge for the third party service.



# Title Services

- Title insurance commissions paid to individual agents must be separately disclosed.
- If party other than title company listed on line 1101 of the HUD-1 provides services that are separate from providing title insurance (i.e., attorney and settlement or escrow agent services) the title company should separately itemize those services with the total amount paid, to the left of the columns.



# Closing Script

- The loan originator would transmit to the settlement agent all the information necessary to complete the “closing script,” which is an addendum to the HUD-1/1A settlement statement. The settlement agent must read the addendum aloud to the borrower at settlement.
  
- The contents of the closing script include:
  - a comparison of the loan terms and settlement charges estimated on the GFE with those on the HUD-1
  - an explanation whether or not charges are within the tolerances
  - a description of the detailed loan terms for the specific mortgage loan as stated in the mortgage note and related settlement information.



# Average Cost Pricing

- The proposed rule would permit charges for third party services to be calculated using average cost pricing mechanisms based on appropriate methods established by HUD, without violating Section 8.
- The charge for a third party services may be based on the actual average price for that service in all loans closed by the loan originator, on a national or more limited basis, during the averaging period.
- The charge may also be based on a tiered pricing contract, provided the projected number of loans used in calculating the average is equal to the number of loans actually closed by the loan originator during the averaging period.



# Clarifies the Treatment of Discounts

- Amends the definition of a “thing of value” to provide that a “discount negotiated by settlement service providers in the price of a third party settlement service is not a thing of value, provided that no more than the discounted price is charged to the borrower and disclosed on the HUD-1/1A.”



# Builder Incentives

- The definition of “required use” would be amended to mean:
  - a situation in which a borrower’s access to some distinct service, property, discount, rebate, or **other economic incentive, or the borrower’s ability to avoid an economic disincentive or penalty**, is contingent upon the borrower using or failing to use a referred provider of settlement services.
- The offering by a settlement service provider of an optional package or a combination of bona fide settlement services to a borrower at a total price lower than the sum of the prices of the individual settlement services does not constitute a “required use.”



# Effect on Other Laws

- GFE application would trigger early TILA disclosures
- Unclear whether a GFE application would trigger HMDA reporting, although arguably such a small amount of data could be treated as a “prequalification” rather than an application.
- Rejection of a GFE application, however, would likely be treated as an adverse action under ECOA and FCRA.
- The new denial notice is inconsistent with the ECOA and FCRA requirements for adverse action or counteroffer notices.
- Argument that the borrower’s intent merely to request a GFE for shopping purposes may be insufficient to allow the originator to pull credit under FCRA without the borrower’s consent.



# Miscellaneous Proposals

- Eliminates the 1% (2.5% for new construction) cap on FHA origination fees
- Updates the Servicing Transfer Disclosure match previous statutory changes
- All RESPA disclosures may be provided to consumers in electronic form so long as the consumer consents and other applicable ESIGN conditions are met



# Questions & Answers

Any further questions may be submitted electronically to:

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