The New RESPA Rules and the Good Faith Estimate:
A Guide for Title Insurance Providers

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For many of us in the title insurance industry the Good Faith Estimate (hereinafter the GFE) has, until now, been something in the nature of a tree falling un-witnessed in the forest. The title report has been ordered and the closing scheduled so we assume the GFE has been provided to the borrower even though we did not see it happen and were oftentimes not directly involved in producing it. Providing the GFE to the borrower has been and, under the revised rules codified at 24 CFR Parts 203 and 3500, "Real Estate Settlement Procedures Act (RESPA): Rule to Simplify and Improve the Process of Obtaining Mortgages and Reduce Consumer Settlement Costs" (hereinafter the "New Rule"), will continue to be the responsibility of the lender or mortgage broker (referred to in this article as the "loan originator" in accord with the terminology used in the New Rule). However, the writing on the wall (and in the law) suggests that we in the title insurance industry are going to find our ability to assist in providing data for the new GFE integral to our lending clients' assessment of our utility as partners in the mortgage settlement process.

Prior to the New Rule a GFE has been just that: an estimate made in "good faith," of the likely settlement costs of a mortgage loan. Under the rules in effect prior to the New Rule, "Each such estimate must be made in good faith and bear a reasonable relationship to the charge a borrower is likely to be required to pay at settlement, and must be based upon experience in the locality of the mortgaged property."[1] The regulations suggested a form in the appendix for lenders to use, but it was not mandatory that the lender use it. As anyone who has shopped for a mortgage can attest, different lenders' good faith efforts to estimate title-related settlement costs which are highly influenced by local geography and local law often result in greatly disparate results. This is not without reason as calculating these costs can be a complex business and, for title producers, it is the subject of audits and government investigation.

However, the New Rule will impose an objective standard as to what shall constitute a "good faith" estimate and it imposes a standardized GFE form that must be used. This objective standard is presented in the form of tolerances. Although some items in the title insurance related portions of the GFE will be allowed to fluctuate slightly from the time of providing the GFE to the time of closing, due to the relatively strict limits of these tolerances, lenders will nevertheless need to provide rather precise figures at a very early stage in the loan origination process. Although lenders are free to use the new GFE form now, and consequently be subjected to all of the New Rule's requirements, "compliance with the new requirements pertaining to the GFE and settlement statements is not required until January 1, 2010."[2]

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[1] §3500.7(C)(2), revised as of January 1, 2007

[2] Final Rule Summary, 68204 Federal Register / Vol. 73, No. 222 / Monday, November 17, 2008 / Rules and Regulations

Under the New Rule, when a lender or mortgage broker receives a mortgage application or information sufficient to complete a mortgage application, the applicant must be provided with a GFE not later than 3 business days after the lender or mortgage broker receives the application or information sufficient to complete one[3], unless before the expiration of this period the lender or mortgage broker denies the application[4] or the applicant withdraws the application.[5] If it is justified (more on that below) a revised GFE may be provided to the borrower after this period, in which case compliance with the tolerances will be determined by comparing the final settlement charges to the revised GFE rather than the original GFE.[6] The estimate of the title-related charges and terms provided on the GFE must be available for at least 10 business days from when the GFE is provided.[7]

There are three basic *categories* of charges and terms on the new GFE: charges that cannot increase, charges that can increase, and charges than can only increase by a maximum of 10% from the figures depicted on the GFE.[8] Assuming that the lender requires certain settlement services (i.e. title insurance), and either the lender chooses the settlement service provider (i.e. the title agent) [9] or the loan originator identifies the provider that is then chosen by the borrower[10] then the charges of that provider / those providers will be grouped together with government recording charges,[11] and together the aggregate sum of these charges at closing cannot exceed ten percent above the sum of the amounts listed on the GFE for those charges.[12]. In the probably rare case where the applicant chooses his/her own title insurance provider and this provider was not identified by the loan originator, then the fees of that provider may increase at closing.[13] In all cases however, transfer taxes (including mortgage taxes), cannot increase at all from the figures depicted on the GFE[14]. For title-related purposes this means that transfer taxes (which include mortgage taxes) must be quoted with total precision and all other title-related charges will be subject to an aggregate 10% tolerance. It is important to note that the 10% tolerance charges may not necessarily all be from a single settlement service provider. Nevertheless the loan originator is responsible for quoting charges for these items and their aggregate sum must remain within the 10% tolerance. If the costs at settlement exceed these tolerances, the loan originator will have the opportunity to cure the tolerance violation by reimbursing the borrower the amount by which the tolerance

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[3] See §3500.7(a)(1) {regarding lender originated transactions} and §3500.7(b)(1) {regarding broker originated transactions}
[4] §3500.7(a)(3)(i) and §3500.7(b)(3)(i)
[5] §3500.7(a)(3)(ii) and §3500.7(b)(3)(ii)
[6] §3500.7(f)
[7] §3500.7(C)
[8] See §3500.7(e)
[9] §3500.7(e)(2)(i)
[10] §3500.7(e)(2)(ii)
[11] §3500.7(e)(2)(iii)
[12] §3500.7(e)(2)
[13] §3500.7(e)
[14] §3500.7(e)(1)(iv) The term "Transfer taxes" includes Mortgage Tax. See item 8 on page 2 of the GFE Instructions: "Transfer taxes: These charges are for state and local fees to records your loan and title documents."

was exceeded, either at settlement or within 30 calendar days after settlement.[15] In states like New York where transfer taxes can vary considerably even from township to township, the consequences for the loan originator of exceeding these tolerances are sobering.

Now if the loan originator is going to be held liable if actual settlement costs exceed the amounts on the GFE and the only mechanism for curing these tolerance violations is for the loan originator to reimburse the borrower it might beg the question, "Why not just provide a revised GFE to the borrower if the tolerances for the charges will be exceeded at final settlement?" The answer is that the right of the loan originator to provide a revised GFE is anything but absolute.

Section 3500.7(f) titled, "Binding GFE", makes this clear. "The loan originator is bound, within the tolerances provided in paragraph (e) of this section, to the settlement charges and terms listed on the GFE provided to the borrower, unless a new GFE is provided prior to settlement consistent with this paragraph (f)."[16] If a revised GFE is provided in accord with paragraph (f) the loan originator must document the reason and retain that documentation for at least three years after settlement.[17] There are six categories of valid reasons for providing a revised GFE: (1) changed circumstances affecting settlement costs, (2) changed circumstances affecting the loan, (3) borrower-requested changes, (4) expiration of the original GFE, (5) interest rate dependent changes, and if an additional disclosure is made to the borrower (6) for mortgage transactions in connection with the purchase of a new home where the purchase is anticipated to occur more than 60 calendar days from the time a GFE is provided.[18]

Of the above categories, "changed circumstances affecting settlement costs" and "borrower-requested changes" appear to be most of concern to title-related service providers because (1) they may require recalculation of title-related charges, and (2) they will trigger the start of a three business day period in which a loan originator will be able to provide a revised GFE to the borrower reflecting these new charges. In regards to the latter category of "borrower-requested changes", the loan originator's duties are straightforward: "If a borrower requests changes to the mortgage loan identified in the GFE that change the settlement charges or the terms of the loan, the loan originator may provide a revised GFE to the borrower."[19] As was said the loan originator has three business days to do this. However, it is the former, "changed circumstances affecting settlement costs", that requires a closer look.

> *Changed circumstances affecting settlement costs.* If changed circumstances result in increased costs for any settlement services such that the charges at settlement would exceed the tolerances for those charges, the loan

[15] §3500.7(i)
[16] §3500.7(f)
[17] Id.
[18] See §3500.7(f) 1 through 6
[19] §3500.7(f)(3)

> originator may provide a revised GFE to the borrower. If a revised GFE is to be provided, the loan originator must do so within 3 business days of receiving information sufficient to establish changed circumstances. The revised GFE may increase charges for services listed on the GFE only to the extent that the changed circumstances actually resulted in higher charges.[20]

The unavoidable question here is therefore, "What would qualify as 'changed circumstances' that would affect settlement costs?" Here is the definition of "changed circumstances" that appears in the New Rule:

Changed circumstances means:

(1) (i) Acts of God, war, disaster, or other emergency;
(ii) Information particular to the borrower or transaction that was relied on in providing the GFE and that changes or is found to be inaccurate after the GFE has been provided. This may include information about the credit quality of the borrower, the amount of the loan, the estimated value of the property, or any other information that was used in providing the GFE;
(iii) New information particular to the borrower or transaction that was not relied on in providing the GFE; or
(iv) Other circumstances that are particular to the borrower or transaction, including boundary disputes, the need for flood insurance, or environmental problems.

(2) Changed circumstances do not include:
(i) The borrower's name, the borrower's monthly income, the property address, an estimate of the value of the property, the mortgage loan amount sought, and any information contained in any credit report obtained by the loan originator prior to providing the GFE, unless the information changes or is found to be inaccurate after the GFE has been provided; or
(ii) Market price fluctuations by themselves.[21]

If this does not make things crystal clear perhaps you will be relieved to hear that HUD promises to provide more guidance on this issue in the future.[22] For now, however, we can glean some insight from the discussion provided by HUD in their November 17, 2008, release of the New Rule. "Changed circumstances that result in higher costs can be a basis for providing a revised GFE. In addition, information that was either not known or not relied on at the time the original GFE was provided may also be the basis for

[20] §3500.7(f)(1)
[21] §3500.2(b)
[22] See Federal Register / Vol. 73, No. 222, 68212: "Additional guidance on what constitutes 'changed circumstances' will be provided by HUD during the implementation period."

providing a modified GFE."[23] Nevertheless certain information will be presumed to have been relied upon.[24]

Compare the treatment of the following two theoretical market price fluctuations found in the November 17, 2008, release of the rule: "If there are changes in the tax rates or in the price of the property after a GFE is provided, those changes would either constitute changed circumstances or new information that would be the basis for providing a revised GFE."[25] However, "if an appraiser that a loan originator intends to use for a particular transaction raises its prices by $50 after the loan originator has already provided a GFE… such a price increase by the appraiser would not be a 'changed circumstance' allowing the issuance of a new GFE." [26] Although the above definition of "changed circumstances" excludes changes in, "the mortgage loan amount sought," from the definition we are nevertheless informed that, "if the actual loan amount turns out to be higher than the loan amount indicated by the borrower at the time the GFE was provided, and certain settlement charges that are based on the loan amount increase as a result, the loan originator may provide a revised GFE reflecting those higher amounts."[27] Of course, though a borrower seeking a new loan amount might not be a "changed circumstance" it would nevertheless be a "borrower-requested change". The point is that what constitutes "changed circumstances" is not settled. Consider the following as a further illustration.

Suppose that a loan applicant in Suffolk County, New York, is current on his mortgage with Bank A. His current balance on that mortgage is $390,000. He is considering a refinance of this mortgage and places an application with his current bank, Bank A, and another bank, Bank B. For ease of calculation, we will assume that he wants to cash out an additional $10,000, and that he will be paying all closing costs out of pocket. A new mortgage in Suffolk County would be subject to 1.05% mortgage tax, with 0.8% payable by the borrower, for a borrower's mortgage tax liability of $400,000 x 0.008 = $3,200. Bank A provides him with a GFE that takes into account recording a new mortgage in the amount of $10,000 and consolidating it with the present mortgage that has a balance of $390,000, thus saving him mortgage tax of $390,000 x 0.008 = $3,120. Bank A also lists consolidation-related charges that add up to several hundred dollars, but the borrower still ends up saving thousands of dollars through the use of a consolidation.

The issue of how Bank B should draft its GFE is not entirely clear. Bank A is not legally obligated to provide an assignment of its mortgage to Bank B so that the borrower (and Bank B) realize a mortgage tax benefit yet it is done routinely, at least in part, because it enables Bank A to charge a fee for providing an assignment whereas it cannot charge for providing a satisfaction. Would it therefore constitute "changed circumstances" if Bank B drafts a GFE assuming the use of a consolidation at application and thereafter finds that Bank A will not assign its mortgage? Or rather, would "changed

[23] Federal Register / Vol. 73, No. 222, 68219
[24] Federal Register / Vol. 73, No. 222, 68220
[25] Federal Register / Vol. 73, No. 222, 68219
[26] Federal Register / Vol. 73, No. 222, 68220
[27] Federal Register / Vol. 73, No. 222, 68220

circumstances" only exist if Bank B assumed that a consolidation was not going to be done and subsequently found out that Bank A was willing to assign the mortgage and for a fee that does not exhaust the mortgage tax benefits? Indeed, in both scenarios nothing has "changed" nor has the lender "required" the use of a consolidation. However, in both scenarios Bank B is placed at a significant disadvantage if it cannot quote for a consolidation-enabled transaction. Finally, since Bank B does not have leverage over Bank A it is unclear how it could ascertain this information within the time constraints the New Rule places upon it.

From a big picture perspective we can see that under the New Rule the loan originators have incurred potential liability for providing quotes that are too low for title-related items. Therefore there is an obvious safety incentive in overestimating these charges. At the same time loan originators will have to balance the desire to avoid liability under the tolerances by overestimating with the business needs of presenting potential borrowers with a "total package" on the GFE that is attractive and that will not cause them to choose another loan originator whose GFE depicts a significantly lower estimate of these charges. After all, a prime purpose of the New Rule is to enable borrowers to price compare.

If loan originators want to provide estimates for title related charges that do not exceed the tolerances while not systematically over-estimating, the loan originators will either need to familiarize themselves with the myriad factors that title insurance providers take into account when pricing settlement services, fees, and taxes, or they will look to our industry to provide these estimates for them with a high degree of precision. The bottle-neck on either approach will likely be available information since in most states applicable title insurance premiums are at least partly dependant upon such factors as the age, vesting, and production of a prior policy and transfer taxes are dependent upon issues such as vesting and the current amount of a pre-existing lien. These factors may not be ascertainable within the three business day period that begins at application. The loan originators may therefore find it desirable to get the borrower to make detailed representations regarding these factors if they wish to provide a more aggressive quote. Should loan originators seek these title-related quotes from their approved providers, these providers may find that they will have to allocate additional resources to meet the demands of a client asking for updated quotes during the mortgage pipeline. Furthermore, due to the precision that will be required, the staff of the title agent that deals with these requests may need to be more highly trained that those who may currently be tasked with communicating with the lender at the title order stage for the providing quotes for the current GFE.

In summary, the GFE under the New Rule will require that loan originators provide quotes that are highly accurate early in the loan origination process and loan originators will be liable for quotes that end up deviating too greatly at settlement. Providing a GFE will continue to be the responsibility of the loan originator but for us in the title insurance industry our tangential relationship with the GFE may be drawing to a close. Loan originators will either have to coordinate with title insurance settlement service providers early and often or they will need to develop their own resources to

provide accurate results of sometimes rather nuanced calculations if they wish to stay within the tolerances. Loan originators have a lot to prepare for and it is safe to assume that our ability to assist them on these quotes will become an important part of their criteria for approved vendors.