

ACORN  
Center for Responsible Lending  
Consumer Federation of America  
Consumer Action  
National Association of Consumer Advocates  
National Community Reinvestment Coalition  
National Consumer Law Center

April 6, 2006

The Honorable Alphonso R. Jackson  
Secretary  
U.S. Department of Housing and Urban Development  
451 7<sup>th</sup> St., SW  
Washington, DC 20410

Dear Secretary Jackson:

Thank you for the opportunity to participate in the RESPA Roundtables held last year. As you know, buying or refinancing a home is generally the largest financial transaction that a family will ever make, and we are glad that HUD is trying to improve the mortgage process. We appreciate your commitment to hearing all views at the Roundtables and we write now to describe the reforms that we believe would most help consumers. These suggestions are grounded in the original and ongoing goals of the mortgage reform process initiated by HUD in the 1990's: to level the playing field for all homeowners obtaining mortgages and to combat the predatory lending that interferes with this process.

In sum, we believe that HUD should take three essential steps:

- **Require that a mortgage broker: (a) reach written agreement with each client early in the financing process on the total amount of the broker's compensation, and (b) provide the consumer with choices regarding how he or she will pay that fee at closing.**
- **Require loan originators to provide an *early and firm* GFE that both itemizes fees and draws attention to important summary information, including an APR alongside the note rate, and loan features such as adjustable rates, prepayment penalties, and balloon payments.**
- **Maintain all section 8 anti-kickback rules, without exemptions.**

**1. Require that a mortgage broker: (a) reach written agreement with each client early in the financing process on the total amount of the broker's compensation, and (b) provide the consumer with choices regarding how he or she will pay that fee at closing.**

In today's marketplace, only the very rare borrower understands the broker's role in a mortgage transaction and the total compensation he will ultimately pay to his broker. The typical borrower would be amazed to learn that the broker he trusted has received extra money (initially from the lender) for placing him in a loan with an unnecessarily high interest rate. However, this practice is now the norm. The yield spread premium is simply an extra fee that the broker extracts from the deal—a fee that the borrower pays, usually several times over, in the form of higher monthly payments. This is exactly the type of kickback that Congress sought to forbid when it enacted RESPA thirty years ago.

HUD should curb abusive yield spread premiums. To achieve real change, HUD must amend its substantive regulations on yield spread premiums; provisions on disclosure would be insufficient. HUD must also reverse its stated prohibition, articulated in its 2001 Policy Statement, against enforcing violations of section 8 through class actions.

On a substantive level, HUD should require brokers to contract with borrowers concerning the specific services they will deliver as well as the total amount to be paid in compensation. Of course, the broker's total fee must be limited to reasonable compensation for those services actually provided to the borrower.

The contracts would work as follows:

- Before any payment is made to the broker, the borrower and the mortgage broker enter into a binding written fee agreement regarding the total compensation, however denominated, to be paid to the broker.
- After loan approval but before settlement, the borrower is offered a choice of how to pay the set broker's fee. The options are to pay cash, to borrow more, or to accept a clearly disclosed increase in interest rate in exchange for having the lender pay the broker's fee. In some circumstances, the borrower may choose a combination of methods.
- The method of payment does not affect the total amount of the broker's fee. Any money paid by the lender to the broker reduces the amount the borrower owes the broker—dollar for dollar. The broker no longer has an incentive to place the borrower in a loan with an interest rate higher than the rate for which he qualifies.

Current practices do not meet these standards. Rather, yield spread premiums now add significant costs to mortgage loans. According to available research, these costs fall particularly hard on the most vulnerable consumers. While loans originated directly by creditors also may include inflated interest rates, the explicit and implicit promises made by brokers to shop for borrowers and represent their interests in the mortgage process

create a special relationship between the broker and the borrower that is not generally mirrored in the strict debtor-creditor relationship when a broker is not involved.

**2. Require loan originators to provide an *early and firm* GFE that both itemizes fees and draws attention to important summary information, including an APR alongside the note rate, and loan features such as adjustable rates, prepayment penalties, and balloon payments.**

HUD should provide for an early, firm and clear GFE to provide certainty for borrowers. Ideally, HUD should format the HUD-1 so that borrowers could easily compare the two forms at closing. This step would help reduce the confusion of borrowers who are generally overwhelmed by today's extremely complex mortgage transactions.

We commend HUD for including information about particularly risky loan features in its sample GFE revision. Presenting borrowers with the highest monthly payment that they could owe under an adjustable-rate loan would help many consumers. Similarly, flagging prepayment penalties and balloon payments would improve upon current disclosures. Shopping solely for the lowest monthly payment available is a recipe for ending up with an unaffordable mortgage. HUD now has the opportunity to help consumers avoid this common mistake.

However, clarifying the GFE and highlighting particular loan features should not mean omitting important detailed information about what consumers are paying for and in conjunction with their mortgage loans. As explained below in our discussion of packaging, enforcement of the Truth in Lending Act (TILA) and the Home Ownership and Equity Protection Act (HOEPA) depend on full itemization of these costs. Changes in the existing requirements for itemization of fees would require additional statutory authorization. Certainly, a summary of critical loan features and costs to the consumer could be included with the more complete disclosure. In addition, APR should be provided alongside a note rate on the GFE so that the consumer easily can identify the effects of the closing costs on the price of the loan.

However, even a perfectly drafted GFE form would not help consumers very much if loan originators were still free to fill in the form with numbers that ultimately had little relationship to final costs. HUD has the authority to determine that the term "good faith" has meaning and that the GFE must be firm. HUD should establish guidelines (similar to the tolerances suggested in past proposals) and should articulate that failure to comply with those guidelines constitutes an unfair and deceptive practice. At least some borrowers harmed by bait-and-switch practices could use such a statement in private enforcement actions.

**3. Maintain all section 8 anti-kickback rules, without exemptions.**

Several large mortgage lenders already offer borrowers bundled services with a single price tag. Under current law, these "packagers" must pass on any volume discounts to the consumer and must steer clear of payments for referrals. HUD's proposal to offer an

exemption from Section 8 would encourage packagers to take a cut of discounts that now benefit consumers directly and would return us to a pre-RESPA world of cost-increasing kickbacks. A Section 8 exemption could also jeopardize the quality of essential settlement services. To increase its profit on a competitively priced package (or to gain more business by undercutting the prices offered by competitors), a lender/packager would have a new incentive to seek the very cheapest services available.

Most significantly, the Section 8 exemption could contribute to predatory lending in the subprime market. The itemization of fees is essential to enforcing compliance with TILA and HOEPA. Litigation over unaffordable and predatory loans frequently focuses on whether the fees charged by the lender have been properly allocated to the calculation of whether the loan is “high-cost” as defined by HOEPA. When a lender has failed to follow HOEPA’s rules for a loan that is later determined to be “high cost,” considerable consumer protections apply. These include enhanced statutory penalties and the option of rescinding the loan. HUD must ensure that nothing it does would allow the concealment of information relevant to TILA disclosures—and HOEPA protections.

Finally, providing lenders “relief” from current requirements in the name of market competition would likely drive prices *up* in the flawed subprime mortgage market—where borrowers have little bargaining power and the conditions necessary for shopping effectively for loans simply do not exist.

We stand with HUD in believing that, by working together, we can greatly improve the mortgage settlement process for all consumers. We would be happy to discuss with you and your staff these proposals or other aspects of HUD’s plans for RESPA reform.

Sincerely,

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