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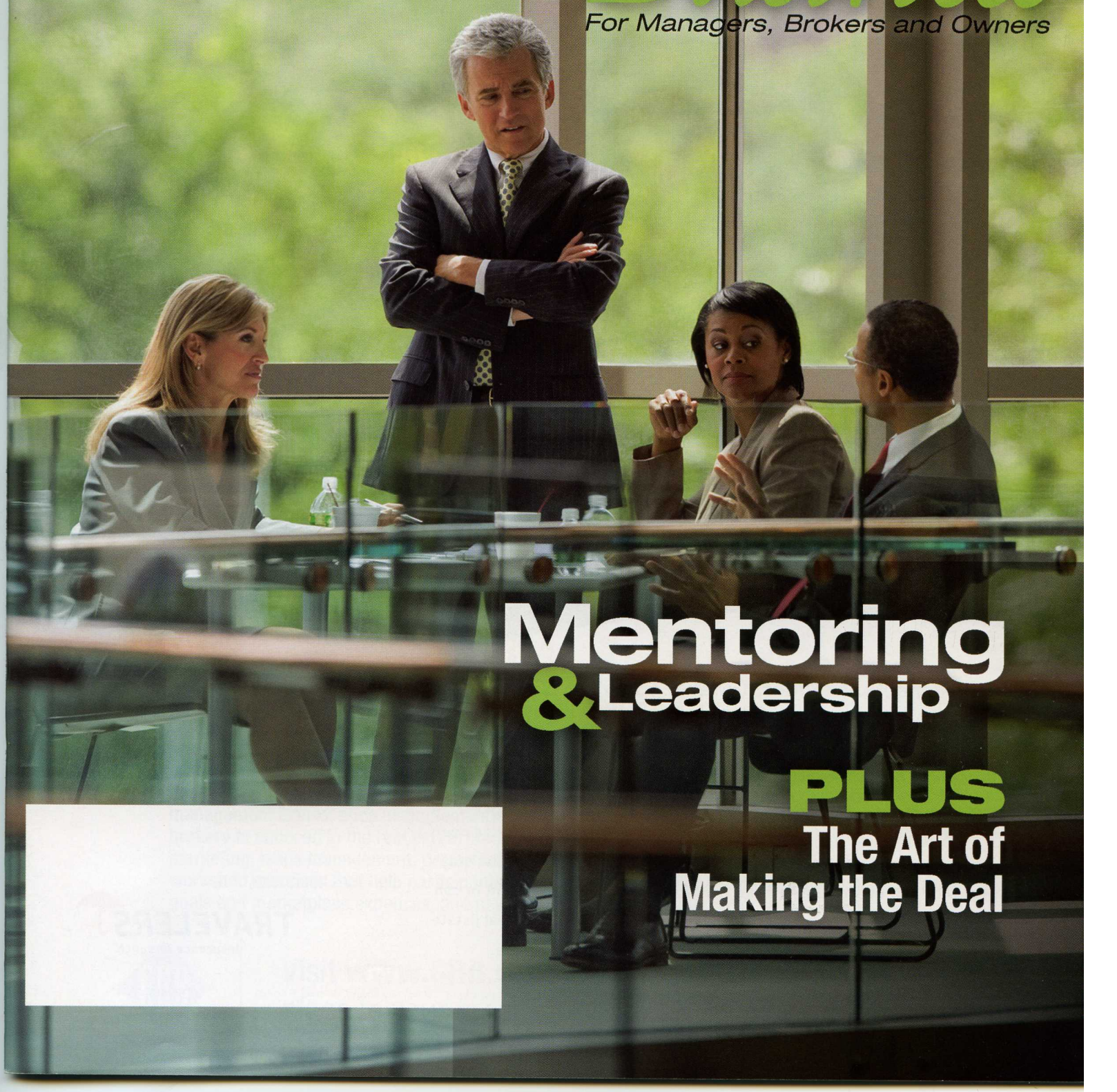

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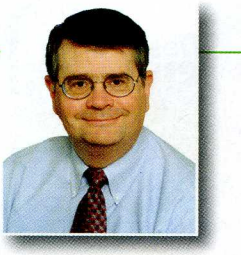
Richard Carlston



RESPA Reform Revisited

Proposed Closing Script continues to be scrutinized.

On March 14, 2008, the U.S. Department of Housing and Urban Development (HUD) released its proposed rule to amend the existing regulations of the Real Estate Settlement Procedures Act (RESPA).[1] HUD's goal is to simplify and improve the disclosure requirements for mortgage settlement costs and to protect consumers from unnecessarily high settlement costs. While few question the desirability of the goals, many question the effectiveness of the proposed rule to accomplish them.

Purpose for the Closing Script

One of the corner pins of the proposed rule is the requirement that the settlement agent (in California, the escrow agent) read to the consumer a Closing Script at the time of closing. The Closing Script is designed to (i) provide the consumer with specific information about the terms of the loan and (ii) provide a comparison of closing costs set forth in the Good Faith Estimate (GFE) and the HUD-1 settlement statement. The goal is to ensure that the consumer understands the principal terms of his or her loan, as well as variances between the estimated settlement costs and the actual settlement costs. However, the method chosen creates serious problems for the title industry and other segments of the market.

As contemplated, the Closing Script is intended to be read to the consumer at the closing, but if the intent is to provide greater transparency and understanding, the consumer should be provided a written form of the Closing Script in advance of the closing. The sooner the script is provided, the sooner the consumer can receive the information and have the opportunity to act on it without also dealing with the voluminous documents and pressures inherent with the closing.[2]

How will the Closing Script be prepared?

The Closing Script is designed to be attached as a new addendum to the HUD-1, and there will be a significant cost to develop the computer software to prepare the Closing Script. The software will need to extract the central loan terms from the lender's computer, the closing costs reflected on the GFE and the closing costs from the HUD-1 to generate the variance report called for by the proposed rule.

Even HUD recognizes that it will be costly to develop the necessary software. Who should bear this cost and how these costs will impact the ability of smaller companies to compete in the marketplace raise serious questions.

Who should prepare the Closing Script?

As proposed, the obligation to prepare the Closing Script rests on the settlement agent, but it is the lender who knows the principal terms of the loan. It is the lender who knows what information was disclosed to the borrower on the GFE. It is the lender who knows the respective variation between costs set forth on the GFE and the HUD-1, which are permissible under the proposed regulation. Accordingly, it is the lender who is in the best position to ensure the accuracy of the information on the Closing Script and who should shoulder that responsibility.

Positing this obligation not only increases the cost of the escrow but significantly increases the potential liability of the escrow. Under existing laws, the duty of an escrow is to follow the instructions that it receives. While some escrow officers may be capable of reviewing loan documentation and retrieving all of the important information (including interest rate information which could be

fixed, adjustable, adjustable with discounts, self-amortizing, etc.) and late fees and penalties, most do not presently have that type of training. Accordingly, positing the responsibility on the escrow will increase the likelihood of improper or confusing disclosures, unnecessarily expand the duties of the escrow and subject the escrow to unnecessary liability.

It may also require the escrow officer to become involved in the unauthorized practice of law. If the escrow officer is to review the loan documentation, interpret the documentation, extract the principal terms, discuss them, address ambiguities and answer questions, it can easily be argued that the escrow officer is engaged in the unauthorized practice of law.

It is clear that the proposed regulation, as currently proposed, would significantly change the role of the escrow.

Is the proposed verbal presentation of the Closing Script at the close of escrow desirable? The proposed rule contemplates that the Closing Script will be read to the borrower at the time of the closing. There are several problems with this proposed requirement. The first and most obvious one is that waiting until the last minute does not facilitate consumer choice. In fact, a common complaint of consumers is the pressure associated with the closing, the volume of documents and the risk of losing their deal if concerns or complaints are registered at the time of the closing. Indeed, by closing with an improper variance, a consumer may be limiting his or her remedy. Requiring the disclosure in writing in advance of the closing would protect the consumer and facilitate consumer understanding.

In addition, this approach does not reflect the reality of our closing marketplace. In California and most states using escrows, escrows are not generally closed with a face-to-face meeting. Rather, the parties to the escrow generally go to the escrow office to sign their documents in advance of the closing, which takes place later without either party being present. Also, there are a large number of escrows signed using an approved third-party signing service. Finally, there are Internet escrows that incorporate e-signatures. Under each of these formats, the marketplace does not contemplate a face-to-face closing, let alone the verbal reading of the Closing Script at the close.

Use of the Closing Script as proposed will delay closings

HUD recognizes that requiring the escrow officer to read the Closing Script will take some time and delay the closing. HUD estimates that the amount of additional time will only be approximately 15 minutes. But in determining its estimate, HUD has failed to include sufficient time for consumer questions. Depending on the inquiry, the prudent escrow officer will need to contact the lender for the requested information. This takes time. Depending on the nature of the inquiry and the availability of the appropriate loan officer, this could take hours. If the closing is happening at the end of the day, it may need to be delayed until the next day. If the lender is not available, the consumer will be presented with the choice of closing the escrow without having received the answer or delaying the close until contact can be established with the lender and the answer retrieved.

Conclusion

Currently, HUD is evaluating each of the foregoing concerns. Ideally, HUD will further amend the proposed rule to require the lender to prepare the Closing Script, provide it in written form a reasonable time in advance of the closing and answer consumers' questions.[3]

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[1] 73 Fed. Reg. 14030 et seq.

[2] Given that variance information is included in the Closing Script, average valuations will need to be provided for some of the cost elements whose exact amount is not known until the closing, such as recording fees.

[3] See, 5/13/08 Comment letter of the American Land Title Association; 6/5/08 Comment letter of the California Land Title Association; 6/10/08 National Association of Insurance Commissioners (Concurs with reading at closing but suggests prior written presentation to consumers; 6/11/08 Comments of the Federal Trade Commission; 6/13/08 Comment letter of the Federal Reserve System (suggesting further testing and noting practical difficulties with the script); 6/11/08 Comment letter of the Small Business Administration.