Testimony of

America's Community Bankers

on

Simplifying the Home Buying Process: HUD's Proposal to Reform RESPA

before the

Subcommittee on Housing and Community Opportunity

of the

Committee on Financial Services

of the

U.S. House of Representatives

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and

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Good afternoon. Chairman Ney, Ranking Member Waters, Distinguished Members of the Committee, thank you for the opportunity to testify at today's hearing on the Department of Housing and Urban Development's proposed rule on the reform of the Real Estate Settlement Procedures Act implementing regulation.

My name is D. Russell Taylor, President and CEO of The Rahway Savings Institution in Rahway, New Jersey. In addition, I am the Chairman of America's Community Bankers. America's Community Bankers represents the nation's community banks of all charter types and sizes. ACB's member banks originate more than 25 percent of all mortgages in the United States, and significantly more than half of all mortgages originated by depository institutions. In addition, ACB members operate a large number of mortgage banking affiliates that originate a substantial part of the business from that segment of the industry.

The Rahway Savings Institution is a New Jersey chartered mutual savings bank with $375 million in assets. As one of New Jersey's oldest financial organizations, it has endured the Great Depression of the 1930's and remained a stronghold throughout the troubled period for banking in the 1980's. We take great pride in the fact that we are local enough to provide personalized attention to our customers, but large enough to offer them the wide range of banking products and services they need. We look forward to serving all of our customers' financial needs--which includes an integral role in providing access to homeownership.

Homeownership is important to every member of America's Community Bankers. The nation's homeownership rate was a record 67.9 percent in 2002, up from 67.8 percent the year before. Last year, the African American homeownership rate increased to 47 percent and the Hispanic homeownership rate increased to 48 percent. ACB members are working hard to increase homeownership rates across the country, which begins with our lenders financing mortgages.

Mortgage finance is a primary business line of the majority of ACB members.
We have members who sell all of their loan originations into the secondary market, members who retain all loans originated in portfolio, and members who do both. Because the membership is nationwide, many members are subject to local laws and regulations that may conflict with elements of HUD's proposal. Any changes to the disclosures or to any aspect of compliance with RESPA will have a significant impact on the business of ACB member institutions.

ACB has been an active advocate of and participant in the mortgage reform debate. We welcome changes to the current disclosures that will provide consumers with a measure of certainty and clarity, because we must increase the homeownership rate so that ALL Americans will be able to own a home, if they so choose.

For this reason, ACB welcomes the opportunity today to comment on the proposal issued by HUD to amend Regulation X, the regulation implementing RESPA.

ACB commends HUD's efforts to reform the mortgage process. Secretary Martinez and the HUD staff should be applauded for taking this important first step to amend the regulation and required disclosures. We appreciate that some of our earlier suggestions have been reflected in the proposal. ACB believes that current requirements are extremely burdensome and do not provide consumers with information that is easily understood or as useful as it might be. The compliance burden of current regulations is very high and any change will require costly and time-consuming modifications to systems and operations.

Although any new regulation also likely will be costly and burdensome for lenders, we hope that ultimately this regulation will reduce costs for consumers and lenders alike. However, insured depository institutions subject to examination and supervision will be required to comply quickly and accurately. As a result, ACB asks for a sufficient transition period for the implementation.

Summary

ACB offers the following specific suggestions, which we believe will make the rule more workable for all industry participants, while fulfilling HUD's goals and the principles established by the Secretary.

On the three areas of the proposal, ACB generally supports the concept of the Guaranteed Mortgage Package and the concept of requiring mortgage broker disclosures. However, we strongly urge HUD to reconsider making changes to the Good Faith Estimate contemporaneously with introduction of the Guaranteed Mortgage Package. We believe that making all of these changes at the same time would unnecessarily disrupt the mortgage market.

We would like to make the following additional comments.

- The proposed mortgage broker disclosures are necessary for consumers to understand the manner in which brokers receive compensation for services provided. Providing this information is essential to decision-making and should be part of any financial literacy efforts;

- HUD must include a reasonable transition period in any changes that are made;

- There are a number of consumer protection laws that contain requirements that are duplicative of or conflict with the proposal. In particular, proposed RESPA changes must be coordinated with Truth in Lending Act requirements;

- HUD must work with the federal banking agencies to ensure that supervision, examination and accounting concerns can be addressed without adversely affecting the ability of insured depositories to offer mortgage products; and

- RESPA must be enforced vigorously by HUD uniformly across affected institutions.

Mortgage Broker Disclosures

ACB believes that the addition of mortgage broker fee disclosures is an important element of mortgage reform. We support HUD in its efforts to require this disclosure and we do not believe that potential delays in other elements of the proposal should result in a delay in requiring this disclosure. Fees charged by mortgage brokers are frequently misunderstood by consumers. We urge HUD to include an easy to understand mortgage broker disclosure requirement in any final rule that is issued.

ACB and other groups in the mortgage-lending arena sent a letter of support for improved fee disclosures after the issuance of the statement of policy in October 2001. As part of that letter of support, ACB and other organizations suggested a method of requiring mortgage broker disclosures. A copy of the letter and the suggested model disclosure form are in the appendix to this written statement.

The Guaranteed Mortgage Package and the Good Faith Estimate of the proposal must be separated

ACB supports the option of the Guaranteed Mortgage Package but we strongly believe that the current good faith estimate must remain an alternative for those lenders who do not wish to package or are unable to do so. As important as it is that consumers be able to comparison shop for mortgage credit, lenders must be able to offer an array of products to meet varying needs of the customer and to give consumers disclosures that are meaningful.

Most importantly, ACB believes that small-to medium-sized lenders are an integral part of the mortgage process and that it is imperative that they be able to be a part of the packaging option to the extent they wish. We believe that many community banks will be able to work with third parties in their local communities to offer an attractive package.

However, it may be that the optimal way for smaller institutions to participate in the packaging option may be for a third party to coordinate, subcontract or otherwise negotiate and arrange the Guaranteed Mortgage Package. We believe that the exemption from Section 8 liability should extend to the activities currently permitted pursuant to HUD’s policy.

If the Guaranteed Mortgage Package succeeds, it will be because the market is ready for such an alternative and it is found to be a meaningful shopping tool by consumers. The experiment also will succeed if lenders and other companies are able to put together packages in an efficient and cost effective manner. However, given the vast array of mortgage products, even those lenders who package may not be able to provide all of the options that consumers need. Each of these concerns may limit the viability of the Guaranteed Mortgage Package. The only fair way to determine if it will work is to try the alternative, while allowing lenders who do not wish to package to use the current mortgage origination process.

ACB strongly believes that implementing the Guaranteed Mortgage Package, while attempting to significantly change Good Faith Estimate procedures at the same time, would create undo stress on the mortgage markets.

Guaranteed Mortgage Package

The proposed Guaranteed Mortgage Package arguably would provide consumers the easiest method of comparison-shopping because it will require a lump sum price for all loan originator and governmental required settlement costs associated with obtaining a mortgage, combined with a "so-called" interest rate guarantee for the loan.

However, we are concerned that providing a "so-called" interest rate guarantee that is held open for a minimum of 30 days as part of the package would not work. We understand that the rate may move based on an index or other observable market changes, but requiring an interest rate guarantee of this sort may lead to confusion on the part of the consumer. The lender will have to develop a method of establishing the rate and determining whether it will change in a manner that will be easily understood by the consumer so that he or she can assess the comparative benefit of the package as time goes on until the rate lock occurs. We suggest that HUD work with lenders of all types to develop a methodology for establishing and adjusting rates. It is important that all types of mortgage lenders be part of this discussion. Some large mortgage lenders maintain or use a readily recognizable index, but smaller lenders or those that retain loans in portfolio may not have an easily understood index.

This concern is exacerbated by the length of time the Guaranteed Mortgage Package is to remain open. The proposal requires the offer to remain open for a minimum of 30 days. We believe that this period of time is much too long. Most home purchase contracts require that financing be applied for within five days.

Another concern is that of conflicts with state law. There are approximately 40 states in which the Guaranteed Mortgage Package may not be able to be implemented for a variety of reasons. We are aware that some of the services to be provided in the package are not permitted by some of the entities that HUD and industry participants envision may become packagers. For example, in some states mortgage brokers are not permitted to give documents containing the annual percentage rate. Also, there are states that have state RESPA and Truth in Lending statutes that must be considered. In my state, New Jersey, borrowers have a right to select the settlement attorney of their choice, possibly upsetting the packaging approach. ACB suggests that HUD look at the differences in how closings are conducted from state to state, and at what different state laws may require. We understand that the method of delivering title insurance and other services varies from state to state. This has an impact on the cost and timing of delivery of the product.

Finally, we agree that entities other than lenders should be able to package and obtain an exemption from Section 8 liability. However, careful consideration must be given to restrictions on the ability of government sponsored enterprises to offer such packages, and whether regulations to prevent loan steering by third party packagers are necessary. Without such restrictions and regulations, the full competitive benefits of RESPA reform are unlikely to be enjoyed by consumers. Further, such regulations may be necessary to prevent an unintended consequence of business being steered away from community lenders.

Good Faith Estimate

The proposed GFE raises a host of compliance and operational difficulties that require significant review and revision before it can be implemented. The changes to the GFE contained in the proposal are sufficiently sweeping that lenders will have to change everything about the way they provide disclosures, resulting in a drastic increase in regulatory burden. If the proposal were finalized as currently drafted, lenders would have the opportunity to offer the guaranteed package, but if they elected not to or were unable to do so, they would still have to change their processes to accommodate the wholesale changes to the GFE.

Additional Concerns of the Proposal

Extended Transition Period Required

An extended transition period of a minimum of several years would be required for many parts of the HUD proposal. The creation of a Guaranteed Mortgage Package will not require such a lengthy phase in period, but it may take that amount of time to resolve some of the state law conflicts. If the GFE is adopted in the proposed form, the transition time required to ensure compliance would be a minimum of two to three years. Lenders would have to amend their requirements, train staff, and check the quality of the disclosures.

Changes must be coordinated with other federal banking agencies

Both the proposed Guaranteed Mortgage Package and the proposed revisions to the GFE contain changes that must be coordinated with the requirements and the definitions of other consumer protection laws that are implemented by regulations promulgated by the Federal Reserve. The most important example of a regulation that must be coordinated with these proposed requirements is Reg Z, the regulation that implements the Truth in Lending Act, and the disclosures required under that regulation. Both the proposed GFE and proposed Guaranteed Mortgage Package require that the APR be disclosed, an element of disclosure required by the Truth in Lending Act. Much of the information required by the proposal is already required by TILA. Currently, the TILA disclosures are given at the same time as the GFE.

The purposes of Truth in Lending and RESPA are different. TILA was enacted to provide consumers with the cost of credit, and RESPA was enacted to provide the costs of settlement. The disclosures required by and definitions used in TILA and RESPA must be coordinated or consumers will be confused by documents that they receive at the same time.

Supervision, Examination and Accounting Conflicts with Federal Banking Agencies

An unintended consequence of the guaranteed rate requirement contained in the Guaranteed Mortgage Package and the proposed GFE is that there may be supervisory or accounting concerns about the treatment of these guaranteed rates. HUD must consult with both accounting standard setters and federal bank regulatory agencies with respect to the guaranteed rate in the Guaranteed Mortgage Package and the GFE. The agencies' analysis of a regulated banking institution may very well be affected by the rate guarantee provision in the proposal, especially in relation to the interest rate sensitivity of the institution in much the same way that agencies would consider a formal loan commitment.

Laws and Regulations Should be Enforced Vigorously

We urge HUD to strengthen its review and enforcement program of lenders who are not otherwise examined and supervised. ACB member institutions are insured depository institutions subject to regular supervision and examination. Examinations include reviews of their policies and procedures, as well as specific transactions.

Financial Literacy is an Important Element of Mortgage Reform

We strongly believe that consumers who know and understand what they are shopping for are the best homebuyers. We believe that education must begin before the consumer makes an application. Homeownership counseling is a crucial step to purchasing a home. According to community bankers responding to ACB's 2003 Real Estate Lending Survey, five to ten percent of community bank loan production is made up of first-time homebuyers, and 64 percent of ACB's members have either required or recommended education and counseling for at least one mortgage or consumer lending product. Education can increase the number of potential borrowers, and counseling can mitigate credit problems.

Conclusion

ACB strongly supports mortgage reform and believes that HUD's proposed RESPA changes are a good start. In order for consumers to benefit from RESPA reform, the rules have to be realistic and workable in the marketplace.

We urge HUD to implement in a timely manner mortgage broker fee disclosures, and separate the implementation of the Guaranteed Mortgage Package from the revised Good Faith Estimate. Mortgage broker fee disclosures are an integral part of making mortgage fees comprehensible to consumers, which is essential to financial literacy efforts. The Guaranteed Mortgage Package, with revisions, should take priority and be tested in the market as soon as practicable. Revisions to the Good Faith Estimate should be postponed, reexamined and adjusted as the Guaranteed Mortgage Package is being tested.

In order for a final rule to be implemented effectively, concerns and conflicts with other federal regulators and banking agencies must be reconciled. Similarly, HUD must address the existence of state laws that frustrate the underlying purpose of the packaging concept. We encourage HUD to apply the safe harbor exemption to HOEPA loans.

ACB members stand ready to work with Members of the Committee and HUD to complete the RESPA reform process in a way that is efficient and feasible.

Thank you for the opportunity to express the views of members of America's Community Bankers.