

October 31, 2008

Honorable Steve Preston, Secretary;
Honorable Gary Cunningham, Deputy Assistant Secretary, Regulatory Affairs and Manufactured Housing;
Ms. Ivy Jackson, Director, Office of RESPA and Interstate Land Sales
U.S. Department of Housing and Urban Development
451 7th Street S.W.
Washington, DC 20410

Honorable Jim Nussle, Director
Office of Management and Budget
725 17th Street NW
Washington, DC 20503

Dear Secretary Preston, Deputy Secretary Cunningham, Ms. Jackson, and Mr. Nussle:

As a coalition of consumer and civil rights organizations, we commend HUD for its groundbreaking work on the summary GFE—a real and significant step forward for consumers. The RESPA Rule has not, to our knowledge, however, adequately addressed three critical issues that we hope HUD will address in its final rulemaking.

Several of our organizations submitted comments to HUD that addressed many elements of its proposal in detail. For purposes of this letter, we focus on three principal concerns we have with HUD's approach, which, in the interest of homeowners, should be addressed. HUD should 1) address abusive yield-spread premiums substantively or, at the very least, improve the origination cost disclosure; 2) coordinate with the Federal Reserve to develop one integrated disclosure form that includes the annual percentage rate (APR); and 3) require that the GFE be binding for at least 30 days and require an interest rate lock of at least 10 days.

1. *HUD must address abusive yield-spread premiums substantively.*

Yield-spread premiums (YSPs)—or payments from lenders to brokers in exchange for the broker selling the borrower a loan with a higher interest rate than the borrower qualifies for— were one of the key drivers of the foreclosure crisis. They encouraged brokers to steer borrowers into risky, expensive loans, and often further encouraged brokers to lock borrowers into those loans by attaching a prepayment penalty that resulted in higher yield-spread premiums.

HUD has clear authority under Section 8 of RESPA to ban abusive YSPs as illegal kickbacks. To date, HUD has allowed YSPs on the theory that consumers can use them to buy down upfront origination costs. The reality, however, is that this trade-off rarely, if ever, occurs, at least when both the borrower and the lender pay the broker. HUD, in the regulatory review accompanying the issuance of the proposed rule, cited extensive evidence that, even in the prime market,

borrowers with YSPs pay in the aggregate more for their loans, in fees, interest, and other closing costs.

As the catastrophic effects of the foreclosure crisis on the global economy increase every day, we find no excuse for HUD's continued failure to ban this abusive practice. HUD must refine its policy position under Section 8 to allow for yield-spread premiums *only* when YSPs are a true trade-off. In order to ensure that YSPs are a true tradeoff, they must be banned except when the borrower pays no origination costs, either out of pocket or from the loan proceeds. Only when all the costs are rolled into the interest rate can YSPs function as envisioned by HUD, as a tradeoff between the interest rate and the closing costs. Otherwise, the total cost of the loan increases. Similarly, YSPs should not be permitted to be coupled with prepayment penalties.

HUD attempted to address YSPs through disclosure. *However, disclosure alone cannot curb abusive YSPs.* In fact, the Federal Reserve Board, which also recently looked at regulating YSPs through disclosure, recognized that its originally proposed disclosure-oriented broker rules were insufficient to curb abuses. Moreover, HUD's proposed origination cost disclosure could ultimately result in more harm than good for consumers. First, it presumes a trade-off between the YSP and upfront costs, which, as we noted, usually does not occur. Second, it refers to the YSP as a credit, which could lead consumers to think they are getting a better deal with a YSP when they are in fact getting a worse deal. Third, it has not been subjected to adequate consumer testing to determine whether borrowers will find it clear and comprehensible. HUD has not tested the key price disclosure, the tradeoff box, and it has done no consumer testing of the typical mortgage decision, a choice between loans that vary both in fees and interest. There is no indication, then, that these disclosures will enable borrowers to choose a more advantageous loan in a real-life situation.

The only way HUD can adequately address abusive YSPs is through substantive reform. Moreover, HUD's proposed disclosure regime is misleading. Broker compensation should be disclosed straightforwardly as "Broker Compensation." In addition, the tradeoff box, while potentially useful for consumers, must be revised in order to prevent deception.

2. *HUD should coordinate with the Federal Reserve to develop one integrated disclosure form consumers can use for shopping, which must include the annual percentage rate (APR).*

Coordination between HUD and the Federal Reserve is long overdue. Consumers should be able to shop for a loan by reviewing all cost components on a single document. This is especially important since settlement costs and the cost of credit are entirely interdependent; disclosing them separately makes it easier for originators to manipulate the distribution of costs between these two "buckets" and make loans that are in fact excessively expensive appear affordable. These coming months, as the Federal Reserve continues its comprehensive review of Regulation Z, are an ideal time for the agencies to work together to develop an integrated approach.

Without integration, HUD's proposal steers consumers to shop based on settlement costs alone when, in reality, settlement costs make up a very small portion of the total loan cost. Including

the note rate on the GFE, as HUD proposes, does not remedy this defect, since the cost of the loan depends on the interplay between settlement costs and the note rate. As proposed, HUD's GFE does not include the only figure that captures all finance charges, whether upfront or charged over time—the annual percentage rate (APR). The only apples-to-apples comparison of loan cost is the APR; any shopping document, therefore, must include it.

Other coordination between the Federal Reserve Board and HUD is also needed, particularly to ensure that average cost pricing and the streamlined GFE and HUD-1 do not obscure the TILA finance charge calculation.

HUD proposed listing some of the riskiest features of the loan on the summary page, including payment increases, negative amortization, balloon payments, escrow status, and prepayment penalties. Coordination with the Federal Reserve should not result in the removal of these important loan terms from the one-page integrated disclosure document.

3. *HUD should require that the GFE be binding for at least 30 days and that the interest rate be locked for at least 10 days.*

Lenders should be able to predict settlement costs with a high degree of certainty for a 30-day period. In fact, settlement costs are unlikely to fluctuate at all within this time. Consumers must have early and binding disclosures in order to have a true opportunity to shop among loan options. As such, the GFE should be binding for at least 30 days instead of 10.

Moreover, HUD absolutely must require an interest rate lock in order for the GFE to be effective. Without a rate lock, consumers must shop on settlements costs alone, which, again, are a relatively small component of total cost. Without an interest rate lock, it is too easy for originators to bait and switch consumers by presenting deceptively low settlement costs, only to recoup those costs by increasing the rate when the consumer returns a few days later. The large majority of prime rate lenders offer a *30-day* interest rate lock, which indicates that (1) the implementation cost of a required rate lock would be minimal; and (2) a 10-day rate lock is more than feasible.

By asking HUD to address these deficiencies, we are not in fact asking it to wait. Rather, we are asking it to proceed on an expedited basis to rein in abusive yield-spread premiums; coordinate with the Federal Reserve and provide the APR on any shopping document; and give consumers a fair chance to shop by requiring the GFE and the interest rate to be binding for reasonable periods of time. We are happy to work with HUD to assist in these efforts and applaud HUD for its important movement to date on much-needed RESPA reform.

Sincerely,

Center for Responsible Lending

Consumer Action

NAACP

National Association of Consumer Advocates

National Consumer Law Center (on behalf of its low-income clients)

National Community Reinvestment Coalition

National Council of La Raza

National Fair Housing Alliance

U.S. PIRG