CLARIFICATION OF MAJOR CHANGES

Integrated Mortgage Disclosures

VISION BEYOND THE NUMBERS

Financial Institutions and Title Industries will see Major Changes from Integrated Mortgage Disclosures.

Introduction

One of the mortgage industry's most anticipated provisions of the Dodd-Frank Act has been the integration of the Truth-in-Lending Act (TILA) and Real Estate Settlement Procedures Act (RESPA) mortgage disclosures. The Consumer Financial Protection Bureau (CFPB) was tasked with the responsibility of implementing this aspect of the law. Since July 2012, the CFPB has been conducting research, testing, and analysis on how best to combine existing mortgage disclosures in a way that would allow consumers to more accurately understand the financial contracts into which they were entering. In late 2013, the CFPB issued the final rule (the Rule)—which becomes effective August 1, 2015—that implements the integration of the TILA and RESPA disclosures.

The Rule creates two new disclosures termed the Loan Estimate disclosure and the Closing Disclosure. The Loan Estimate disclosure takes the place of the RESPA Good Faith Estimate and the initial TILA disclosures, while the Closing Disclosure replaces the HUD-1 Settlement Statement and the final TILA disclosure.

The Rule also streamlines various terms and conditions that were previously found in both RESPA and TILA (as originally implemented in the U.S. Department of Housing and Urban Development's Regulation X and the Federal Reserve Bank's Regulation Z, which were both transitioned to CFPB regulations in accordance with the Dodd-Frank Act). For example, what constituted an application, and thus served as the trigger for certain related disclosures, was different between the two regulations. There were also separate disclosure timing requirements and procedures for changes that exceed established tolerances. This resulted in a great deal of confusion and costs to ensure compliance by creditors. Through integration, conflicting and overlapping definitions and rules should be streamlined.

When to Use the Integrated Disclosures

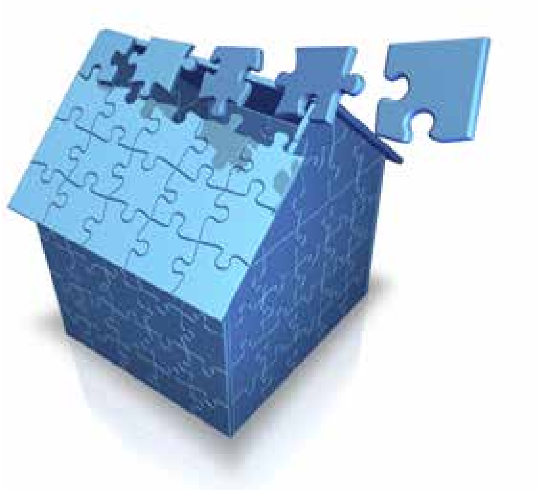
The integrated disclosures will be used for closed-end consumer loans that are secured by real property. Home equity lines of credit, reverse mortgages, or mortgages secured by a mobile home (or other dwelling) that is not attached to land are not subject to the Rule. Existing RESPA and TILA disclosures continue to be required for these type of loans (as applicable). There are certain types of loans that were previously subject to TILA but not RESPA, such as construction-only loans and loans secured by vacant land or by 25 or more acres. These types of credits will be subject to the new integrated mortgage rules.

The *Loan Estimate* disclosure is to be provided to the consumer at least three business days after the creditor receives the loan application. The Rule defines business day for this purpose as any day the institution's offices are open to the public for carrying out substantially all of its business functions. The rule defines an application as the submission of a consumer's financial information for purposes of obtaining a credit. The application must include the following six items:

- Consumer's name.
- Consumer's income.
- Consumer's social security number to obtain a credit report.
- Property address.
- Estimate of the value of the property.
- Mortgage loan amount sought.

The Rule permits an application to be submitted in written or electronic form and also includes a written record of an oral application. There is no requirement that all six pieces of information be obtained at one time. The rule does not prohibit other information from being required by a creditor during the application process. Thus, individual institutions should establish policies and processes to determine the information that will be collected to determine when disclosure requirements will be triggered.

The *Loan Estimate* disclosure must also be delivered no later than the seventh business day before consummation of the transaction.



When to Use the Integrated Disclosures

The *Closing Disclosure* is to be provided for all loans that require a Loan Estimate disclosure and that also proceed to closing. The *Closing Disclosure* must be provided to the consumer no later than three business days before consummation[1] of the loan. Consummation, as defined in the Rule, occurs when the consumer becomes contractually obligated (dependent on State law) to the creditor on the loan. If the *Closing Disclosure* is provided to the consumer in person, it is considered to be received the day it is provided. However, if the disclosure is provided via mail or electronically, it is considered to have been received three business days after it is delivered. If the creditor has evidence that the consumer received the *Closing Disclosure* that was sent via U.S. Postal mail or electronically, the institution can consider the disclosure to have been received on that date. The Rule includes a separate definition for "business day" as it relates to timing for the *Closing Disclosure*. "Business day" is defined as all calendar days except Sundays and legal public holidays.

What is Included on the New Disclosures

Loan Estimate Disclosure

A sample version of the Loan Estimate disclosure can be found at (http://files.consumerfinance.gov/f/201403_cfpb_loan-estimate_model-form-H24.pdf).[2]

The Loan Estimate disclosure is three pages in length. The first page includes information on the loan's terms, projected payments, and estimated costs at closing. Much of the information included on this page is straightforward; however, the following are a few unique aspects:

- Loan purpose must be either: purchase, refinance, construction, or home equity loan.
- Loan product must include any payment feature that may change the periodic payment (i.e., interest only, balloon payment, negative amortization, etc.) and the duration of the relevant payment feature. Also, how the interest rate is determined must be included (i.e., adjustable rate, step rate, fixed rate). Thus, a fixed-rate loan with a balloon payment at 5 years would be disclosed as 5-Year Balloon, Fixed Rate, or an adjustable-rate loan that is fixed for 3 years and adjusts annually thereafter, with a balloon payment in 7 years would be disclosed as 7-Year Balloon, 3/1 Adjustable Rate.

[1] It is important to note that consummation of the loan and loan closing (or settlement) are legally distinct events. Consummation, as defined in the Rule, occurs when the consumer becomes contractually obligated (dependent on State law) to the creditor on the loan.

[2] This is a blank model Loan Estimate that illustrates the application of the content requirements in 12 CFR § 1026.37. This form provides two variations of page one, four variations of page two, and four variations of page three, reflecting the variable content requirements in 12 CFR § 1026.37. Therefore, for illustrative purposes, note that our page-by-page analysis herein treats this form as only three pages.

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- The fully indexed interest rate must be used in the projected payment portion if the rate at consummation is not known and there is not an introductory fixed-rate period.

- When any of the following events occur during the life of the loan, a separate column in the projected payments portion should be added (but not more than four columns):
    - o Change in the principal and interest payment amount (i.e., interest-only period ends, interest rate can adjust, or changes due to negative amortization features).
    - o Balloon payments.
    - o Lender-required termination of mortgage insurance (or an equivalent).

The **second page** details costs associated with the loan, a breakout to calculate the cash required to close the loan, and tables for details on adjustable payments and/or adjustable interest rates. The disclosure classifies closing costs as either Loan Costs or Other Costs. Loan Costs include "origination charges," "services [the borrower] can shop for," and "services [the borrower] cannot shop for." Other Costs include taxes and other government fees, prepaid fees (such as homeowner insurance premiums, prepaid interest, property taxes, etc.), and initial escrow payment at closing.

The adjustable payment table is only included when the periodic principal and interest payment changes after consummation, but not because of a change to the interest rate. Thus, the table would be included for loans with interest-only periods or a step or seasonal payment feature as an example. The adjustable interest rate table would only be included if the loan's interest rate can change after consummation.

The **third page** includes several clauses and generic statements related to the contractual aspects of the loan (i.e., assumption clause, servicing intent, late payment fees, etc.). It also includes three measures which are considered helpful for the consumer to compare costs of various loan offers. These measures include:

- *In 5 years* – the total amount of principal, interest, mortgage insurance, and loan costs paid during the first 5 years of the loan.

- *Annual Percentage Rate (APR)* – the APR as calculated based on CFR Part 1026.22 and appendix J to Regulation Z.

- *Total Interest Percentage (TIP)* – the total amount of interest that the consumer will pay over the loan term, expressed as a percentage of the loan amount.

What is Included on the New Disclosures

Each of the measures are required to be calculated assuming all payments will be made, in accordance with the contractual terms, in full and on time. Further, for adjustable rate loans, the measures must be calculated assuming interest rates will increase at the maximum amount permitted by the loan terms.

There is also a portion for the consumer to sign and date which indicates that the disclosure was provided by the creditor. The Rule does not require that a signature be obtained; however, if the *Confirm Receipt* table is not used by the creditor, the statement, "You do not have to accept this loan because you have received this form or signed a loan application," must be included at the end of the Other Consideration table on this page.

Closing Disclosure

A sample version of the *Closing Disclosure* can be found at (http://files.consumerfinance.gov/f/201403_cfpb_closing-disclosure_cover-H25A.pdf).[3]

The *Closing Disclosure* is five pages. The first page of the Closing Disclosure is primarily consistent with the **first page** of the *Loan Estimate* disclosure. Information disclosed should be consistent with the *Loan Estimate* disclosure requirements, but updated based on the final contractual terms.

The **second page** details the *Loan Costs* and *Other Costs* in separate columns for borrower-paid, seller-paid, and paid by others. Items generally should be the same as they were disclosed on the *Loan Estimate* disclosure. However, the following are specific circumstances when services are to be grouped as *Services Borrower Did Not Shop For* regardless of where they were grouped on the *Loan Estimate*:

- Items the consumer could have shopped for, but did not.
- Service providers selected who were listed on the *Written List of Providers*.

The **third page** includes two tables, which are labeled *Calculating Cash to Close* and *Summaries of Transactions*. The *Calculating Cash to Close* table includes a column for the amount from the *Loan Estimate* disclosure and *Closing Disclosure* as well as an area to indicate if the amount changed, and reference to where the amount changed, on the *Loan Estimate*. If there was an increase in closing costs that exceed tolerance limits, a statement should be included outlining such excess above tolerance, along with reference to an associated *Lender Credit* on page two of the *Closing Disclosure* that cured the tolerance violation. The *Summaries of Transactions* table is similar to the first page of the HUD-1 Settlement Statement, and provides

[3] This is a blank model Closing Disclosure that illustrates the content requirements in 12 CFR § 1026.38. This form provides three variations of page one, one page two, one page three, four variations of page four, and four variations of page five, reflecting the variable content requirements in 12 CFR § 1026.38. This form does not reflect modifications permitted under 12 CFR § 1026.38(t). Therefore, for illustrative purposes, note that our page-by-page analysis herein treats this form as only five pages.

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details associated with the real estate transaction between the consumer and seller.

The **fourth page** includes several clauses and statements related to the contractual aspects of the loan similar to page three of the *Loan Estimate* disclosure. Also included on this page are adjustable payment and adjustable interest rate tables, which are consistent with those included on page two of the *Loan Estimate* disclosure.

The **fifth page** has four groupings, which include *Loan Calculations, Other Disclosures, Contact Information* and a place for the consumer to acknowledge receipt of the disclosure. The first four required disclosures in the Loan Calculation portion are consistent with what has been required on the TILA disclosure and include: *Total of Payments, Finance Charge, Amount Financed, and Annual Percentage Rate*. The TIP is also included, which is consistent to the measurement amount included on the *Loan Estimate* disclosure. Also consistent with the Loan Estimate disclosure, the creditor may use the *Confirm Receipt* area to require the borrower to sign and date to acknowledge receipt of the disclosure. However, if a signature is not required by the creditor, the statement, "You do not have to accept this loan because you have received this form or signed a loan application," must be included in the *Other Disclosure* portion on this page.

Conclusion

In preparation for the Rule becoming effective, creditors and title/settlement companies should coordinate with software vendors to ensure compliance will be achieved with the new disclosures. Testing should be conducted to verify that information is accurately disclosed. In addition, financial institutions should evaluate lending processes in light of the regulatory changes. The CFPB also has produced resources, which are located at (http://www.consumerfinance.gov/regulatory-implementation/tila-respa/#disclosures), to assist in understanding and complying with the Rule.

For further details on the changes related to the Rule or to discuss how PYA can assist your institution in the areas of regulatory compliance, contact:

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