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Coming Soon: New Closing (No, Consummation) Rules!

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What?! We can't call it a closing anymore? Under new federal regulations regarding the Truth in Lending Act ("TILA") and the Real Estate Settlement Procedures Act ("RESPA"), the terminology for a "closing" or "settlement" is now a "consummation", a "borrower" is now a "consumer", the HUD-1 Settlement Statement is going away, and the substitute form, called the Closing Disclosure, needs to be delivered to the consumer 3 business days before consummation. The changes were slated to begin on August 1, 2015, but the Consumer Financial Protection Bureau ("CFPB"), which enforces these regulations, recently issued a final rule on July 20, 2015 extending the date to October 3, 2015 instead.

Many residential lenders and settlement agents, as well as real estate agents and brokers, are starting to embrace and prepare for these changes. Builders should also become aware of these new rules because the timing of disclosures forms and certain changes to the forms can affect when consummation occurs. A delay in the effective date, however, will provide the mortgage financing and construction industry more time to prepare for the transition so that upcoming settlements (or rather consummations) will not be painful for borrowers/consumers.

What are these new rules?

To protect consumers from a repeat recession, Congress enacted the Dodd-Frank Wall Street Reform and Consumer Protection Act ("Act"). The Act not only created the CFPB as a new federal agency to enforce consumer protection laws but also directed the CFPB to integrate mortgage loan disclosures under TILA and RESPA. In 2013, the CFPB issued the new TILA-RESPA Integrated Disclosure ("TRID") rule, which integrates 4 separate disclosure forms into 2 forms, provides timelines as to when lenders deliver them to the consumer, and sets different tolerances for changes to the forms.

For the first form, the Good Faith Estimate and the initial Truth-in-Lending disclosure have been combined into one form, called the Loan Estimate. The Loan Estimate discloses information about the costs and risks of the mortgage loan. Lenders are required to deliver the Loan Estimate to consumers 3 business days after the consumer has submitted a loan application to the lender. The Loan Estimate is easier for consumers to learn information about their mortgage loan. For example, if a consumer has a variable interest rate, the form will now disclose the changes in payments over the life of the loan. The new rule also dictates certain tolerance levels as to how much the Loan Estimate can change by the time closing (or consummation) occurs. For example, there is zero tolerance for changes to lender and mortgage broker charges.

For the second form, the HUD-1 Settlement Statement and the final Truth-in-Lending form have been combined into the Closing Disclosure form, which is to be provided to the consumer 3 business days before consummation instead of a day before or at closing. A new 3-day waiting period (and delay in consummation) will be required if the applicable percentage rate increases by more than 1/8 percent for fixed-rate loans and 1/4 of a percent for variable-rate loans, if the loan product changes (such as fixed-rate to variable), or if a prepayment penalty provision is added.

Do these changes also affect construction loans?

Yes. Previously, construction only loans were exempt from RESPA but with the new rule, these loans are no longer exempt. In addition, the new rule was recently revised with respect to new construction loans so that lenders may state on the Loan Estimate that a revised form may be provided where the lender reasonably believes that consummation will occur more than 60 days after the initial Loan Estimate is given. This revision allows lenders to accommodate changes in estimated charges and therefore is an exception to the tolerance levels.

What are the penalties if someone violates the new rule?

The penalties range from up to $5,000 a day for any violation of a law, rule or final order or condition imposed in writing by the CFPB; up to $25,000 per day for any person that recklessly engages in a violation of a federal consumer financial law; and up to $1,000,000 per day for any person who knowingly violates a federal consumer financial law. The CFPB has the power to enforce the new TRID rule and is currently enforcing consumer financial laws, such as the affiliated business arrangement laws. The CFPB has been diligent in enforcing current laws and regulations so this trend will more likely continue with the new TRID rule.

How should the mortgage industry prepare for the changes?Lenders, realtors, title agents, and builders should have their paperwork ready at least a week in advance of closing/consummation to avoid surprises and delays. Some realtors are also anticipating a 2-step inspection process to avoid major changes to the Closing Disclosure form at closing. More importantly, communication among the parties early in the process will be the key to a smooth transaction. To learn more about the new forms, visit the CFPB website: www.consumerfinance.gov/knowbeforeyouowe. A copy of the of CFPB's press release regarding the extension date can be found here.

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