CARLTON FIELDS

The TRID Rule: Impact and Consequences on the Residential Mortgage Lending Market

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Introduction and Background Residential mortgage lenders have long been required to disclose to their borrowers (i) the cost of credit to the consumer and (ii) the cost to the consumer of closing the loan transaction. These regulatory disclosure requirements arise from two statutes – the Real Estate Settlement Procedures Act of 1974 (RESPA) and the Truth In Lending Act (TILA). The regulations were designed to protect consumers by disclosing to them the costs of a mortgage loan (TILA) and the cost of closing a loan transaction (RESPA). These disclosures have in the past been enforced by multiple federal agencies (the Federal Reserve Board, Housing and Urban Development, the Office of Thrift Supervision, the Federal Trade Commission, the Federal Deposit Insurance Corporation, the Office of the Comptroller of the Currency, and the National Credit Union Administration) and provided to consumers on multiple forms with sometimes overlapping information (the Truth in Lending disclosures, the Good Faith Estimate, and the HUD-1 Settlement Statement). **The Dodd Frank Act and CFPB** In 2010, the Dodd Frank Wall Street Reform and Consumer Protection Act (the Dodd Frank Act) created the Consumer Financial Protection Bureau (CFPB), consolidated the consumer protection functions of the above-federal agencies in the CFPB, transferred rulemaking authority under the statutes to the CFPB, and amended section 4(a) of RESPA and section 105(b) of TILA requiring CFPB to issue an integrated disclosure rule, including the disclosure requirements under TILA and sections 4 and 5 of RESPA. The purpose of the integration was to streamline the process and ensure that the disclosures are easy to read and comprehend so that consumers can "understand the costs, benefits, and risks" associated with mortgage loan transactions, in light of the "facts and circumstances." 12 U.S.C. 5532(a). **The TRID Rule** The CFPB issued a propose rule in July, 2012. The final TILA-RESPA integrated disclosure (TRID) rule was published in late 2013, amended in February, 2015, and went into effect on October 3, 2015. More than simply streamlining the existing process, the TRID rule replaced the entire disclosure structure, changing the form, timing, and content of the disclosures. **Scope** – The TRID rule applies to most closed-end consumer mortgages, but not to home equity loans, reverse mortgages, or mortgages secured by anything other than real property (dwellings, mobile homes, etc). It does not apply to lenders who make five or less mortgage loans a year. It does, however, apply to most construction loans that are closed-end consumer credit transactions secured by real property, but not to those that are open-end or commercial loans. **Forms** – The TRID rule replaced the forms that had been used for closing mortgage loans with two new, mandatory forms. The **Loan Estimate** or H-24 form (attached as Exhibit 1) replaces the former Good Faith Estimate and the early TILA disclosure form. The **Closing Disclosure** or H-25 form (attached as Exhibit 2) replaces the HUD-1 Settlement Statement and the final TILA disclosure form. **Content** – Among other information, the three page Loan Estimate must contain (i) the loan terms, (ii) the projected payments, (iii) the itemized loan costs, (iv) any adjustable payments or interest rates, (v) the closing costs, and (vi) the amount of cash to close. If actual amounts are not available, lenders must estimate. Among other information, the Closing Disclosure must contain (i) loan terms, (ii) projected payments, (iii) loan costs, (iv) closing costs, (v) cash to close, and (vi) adjustable payments and adjustable rates as applicable. The required forms are rigid and require the disclosure of this information in a detailed and precise format. **Timing** – The TRID rule requires a creditor (or mortgage broker) to deliver (in person, mail or email) a Loan Estimate (together with a copy of the CFPB's Home Loan Toolkit booklet) **within three business days** of receipt of a consumer's loan application and no later than seven business days before consummation of the transaction. A loan application consists of six pieces of information from the consumer: (i) name, (ii) income, (iii) social security number, (iv) property address, (v) estimated value of property, and (vi) amount of mortgage loan sought. 12 C.F.R. §1026.2 (a) (3)(ii). After receiving an application, a creditor may not ask for any additional information or impose any fees (other than a reasonable fee needed to obtain the consumer's credit score) until it has delivered the Loan Estimate. The TRID rule also requires a creditor (or settlement agent) to deliver (in person, mail or email) a Closing Disclosure to the consumer no later than **three business days** before the consummation of the loan transaction. The Closing Disclosure must contain the actual terms of the loan and actual cost of the transaction. Creditors are required to act in good faith and use due diligence in obtaining this information. Although creditors may rely on third-parties such as settlement agents for the information disclosed on the Loan Estimate and Closing Disclosure, the TRID rule makes creditors ultimately responsible for the accuracy of that information. **Tolerance and Redisclosure** – If a charge ultimately imposed on the consumer is equal to or less than the amount disclosed on the Loan Estimate, it is generally deemed to be in good faith. If a charge ultimately imposed on the consumer is greater than the amount disclosed on the Loan Estimate, the disclosure is generally deemed not in good faith, subject to certain tolerance limitations. For example, there is zero tolerance for (i) any fee paid to the creditor, broker, or affiliate, and (ii) any fee paid to a third-party if the creditor did not allow the consumer to shop for the service. Creditors may charge more than the amount disclosed on the Loan Estimate for third-party service fees as long as the charge is not paid to an affiliate of the creditor, the consumer had is permitted to shop for the service, and the increase does not exceed 10 percent of the sum of all such third-party fees. Finally, creditors may charge an amount in excess of the amount disclosed on the Loan Estimate, without any limitation, for amounts relating to (i) prepaid interest, (ii) property insurance premiums, (iii) escrow amounts, (iv) third-party service providers selected by the consumer and not on the creditor's list of providers or services not required by the creditor, (iv) and transfer taxes.[1] If the fees and charges imposed on the consumer at closing exceed the fees and charges disclosed on the Loan Estimate, subject to the tolerance levels, the creditor is required to refund the consumer within 60 days of consummation of the loan. If the information disclosed on the Closing Disclosure changes prior to closing, the creditor is required to provide a corrected Closing Disclosure. An additional three-day waiting period is required with a corrected Closing Disclosure if there is an increase in the interest rate of more than 1/8 of a percent for fixed rate loans or 1/4 of a percent for adjustable rate loans, a change in loan product, or a prepayment penalty is added to the loan. For all other changes, the corrected Closing Disclosure must be provided prior to consummation. If a change to a fee occurs after consummation, then a corrected Closing Disclosure must be delivered to the consumer within 30 calendar days of receiving information of the change. If a clerical error is identified, then a corrected Closing Disclosure must be delivered to the consumer within 60 calendar days of consummation. **Impact on Relationships Between Lenders and Vendors** The TRID rule is detailed and highly technical and the CFPB has published very little official guidance as to the interpretation of the rule. As a result, the various members of the industry are interpreting the rule widely differently and applying it with the according lack of uniformity. An example of the kinds of disagreement arising is the issue of whether the final numbers can be massaged in order to avoid re-disclosure and delivery of a new Closing Disclosure at closing or after. This has led to significant conflicts between creditors and settlement agents as to what the TRID rule requires. Some have described it as a "battle field" with settlement agent's following creditor's varying instructions but documenting "everything." **Impact on Secondary Mortgage Market** The implementation of the TRID rule has also apparently begun to cause delays in closing consumer mortgage loan transactions, with closing times up month over month and year over year since October. Loan originators are also reporting decreases in earnings and attributing some of that decrease to implementation of the TRID rule. Moreover, Moody's has reported that, because some third-party due diligence companies have been strictly applying their own interpretations of the TRID rule in reviewing loan transactions for "technical" violations (i.e., inconsistent spelling conventions and failure to include a hyphen), these firms have found that up to 90% of reviewed loan transactions did not fully comply with the TRID rule requirements. The fact that most of these compliance issues appear to be technical and non- material has not dampened concerns. **MBA Letter** Indeed, these concerns were set forth by President and CEO of the Mortgage Bankers Association David Stevens in a letter to CFPB Director Richard Codray on December 21, 2015 (letter attached as *Exhibit 3*). In the letter, Stevens identified the problem, proposed a possible interim solution, and asked for ongoing guidance. The problem, according to Stevens, is that certain due diligence companies have adopted an "extremely conservative interpretation" of the TRID rule, resulting in up to a 90% non-compliance rate. This could put loan originators in the position of being unable to move loans to the secondary market or having to sell them at substantial discounts, and could ultimately lead to significant liquidity problems. It is also unknown how the government sponsored entities (GSEs) will interpret the TRID rule, and whether they too will adopt such conservative interpretations and ultimately demand loans be repurchased and seek indemnification for the lack of technical compliance. Stevens proposed written clarification on a lender's ability to correct a variety of these technical errors, but also noted a significant need for ongoing guidance and additional written clarifications. **CFPB's Response** On December 29, 2015, Director Cordray responded to Stevens's letter, reassuring him that the "first few months" of examinations would be corrective, not punitive, and focused on whether creditors have made "good faith efforts to come into compliance with the rule." Cordray also noted the GSEs have indicated that they do not intend to exercise repurchase or indemnification remedies where good faith efforts to comply are present.[2] Cordray also addressed the ability to issue a corrected closing disclosure in order to correct "certain non- numerical clerical errors" or "as a component of curing any violations of the monetary tolerance limits, if they exist." Interestingly, in this context Cordray raised the issue of liability for statutory and class action damages, noting that "consistent with existing . . . TILA principles, liability for statutory and class action damages would be assessed with reference to the final closing disclosure issued, not to the loan estimate, meaning that a corrected closing disclosure could, in many cases, forestall any such private liability." Cordray went on to say that, despite the fact that TRID integrates the disclosures in TILA and RESPA, it did not change the "prior, fundamental principles of liability" under either statute and as a result that:

> (i) there is no general assignee liability unless the violation is apparent on the face of the disclosure documents and the assignment is voluntary. 15 U.S.C. §1641(e). (ii) By statute, TILA limits statutory damages for mortgage disclosures, in both individual and class actions to failure to provide a closed-set of disclosures. 15 U.S.C. §1640(a). (iii) Formatting errors and the like are unlikely to give rise to private liability unless the formatting interferes with the clear and conspicuous disclosure of one of the TILA disclosures listed as giving rise to statutory and class action damages in 15 U.S.C. §1640(a). (iv) The listed disclosures in 15 U.S.C. §1640(a) that give rise to statutory and class action damages do not include either the RESPA disclosures or the new Dodd-Frank Act disclosures, including the Total Cash to Close and Total Interest Percentage.

Cordray concluded his letter by noting that "the risk of private liability to investors is negligible for good-faith formatting errors and the like" and that "if investors were to reject loans on the basis of formatting and other minor errors . . . they would be rejecting loans for reasons unrelated to potential liability" associated with the disclosures required by the TRID rule. While the promise of a good faith implementation period and the assurance that TRID does not expand TILA liability to RESPA disclosures offers some comfort to creditors, Cordray's letter is not a compliance bulletin or supervisory memo, was not published in the Federal Register, and does not appear to be an official interpretation of the TRID rule that would bind the CFPB or any court. Moreover, his comments focus primarily on statutory damages and do not take into consideration potential liability for actual damages and, importantly, attorney's fees. **Potential Areas of Liability** Despite these assurances, creditors still must concern themselves with potential liability for TRID violations. The following is list of the main sources of potential liability for TRID violations. **Regulatory (CFPB)** – The CFPB has the ability investigate potential violations via its authority to issue civil investigative demands, a form of

administrative subpoena. 12 U.C.C. §5562(c). Upon a determination of a violation, the CFPB can issues cease-and-desist orders, require creditors to adopt compliance and governance procedures, and order restitution and civil penalty damages. CFPB may impose penalties ranging from $5,000 per day to $1 million per day for knowing
violations.

> (A) First tier - For any violation of a law, rule, or final order or condition imposed in writing by the Bureau, a civil penalty may not exceed $5,000 for each day during which such violation or failure to pay continues. (B) Second tier - Notwithstanding paragraph (A), for any person that recklessly engages in a violation of a Federal consumer financial law, a civil penalty may not exceed $25,000 for each day during which such violation continues. (C) Third tier - Notwithstanding subparagraphs (A) and (B), for any person that knowingly violates a Federal consumer financial law, a civil penalty may not exceed $1,000,000 for each day during which such violation continues.

12 U.S.C. § 5565(c)(2). **Other Governmental Liability** – Creditors could also face potential additional claims pursuant to the False Claims Act and the Financial Institutions Reform, Recovery, and Enforcement Act (FIRREA). **Consumer Actions** – While statutory damages may be limited under TILA to $4,000 in individual suits and the lesser of 1% of company value or $1 million in class actions, that does not account for potential liability for actual damages and attorney's fees. **Contractual Liability** – Absent a specific contractual carve out for technical violations of TRID, originating lenders and creditors may also face potential liability for violation of contractual representations that the loans they are selling were originated "in compliance with law." **Conclusion** The problem with the TRID rule is that, like the legendary metal bed of the Attic bandit Procrustes, it is a one size fits all regulation and industry participants are going to get stretched or lopped in the process of attempting to fit every transaction into the regulation's apparently inflexible requirements. Time may well bring additional CFPB guidance, either in the form of the CFPB's formal, binding interpretations of the rule or in the form of regulatory decisions. Such guidance may then give industry participants a better understanding of how to make and close mortgage loans and avoid liability in process. In the meantime, we can expect further delays, disagreements, and, ultimately, enforcement and litigation. [1] There had been disagreement on whether transfer taxes (property taxes, HOA dues, condominium or cooperative fees) were subject to tolerances or not. On February 10, 2016, in a rare instance, the CFPB issued an amendment to the supplementary information to the TRID rule to correct a "typographical error" and clarify this issue, amending a sentence that had read that these charges "are subject to tolerances" to read that such charges "are not subject to tolerances" (emphasis added). [2] In fact, Fannie Mae and Freddie Mac both issued similar letters on October 6, 2015 advising that "until further notice" they would "not conduct routine post-purchase loan file reviews for technical compliance with TRID," as long as creditors are using the correct forms and exercising good faith efforts to comply with the rule. In these letters, the GSEs further agreed not to "exercise contractual remedies, including repurchase" for non-compliance except where the required form is not used or if a practice impairs enforcement of the loan or creates assignee liability and a court,

regulator, or other body determines that the practice violates TRID. Similarly, the Federal Housing Administration issued a letter that “expires” April 16, 2016, agreeing “not to include technical TRID compliance as an element of its routine quality control reviews,” but noting that it does expect creditors to use the required forms and use good faith efforts to comply with TRID.

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