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DEPARTMENT OF HOUSING AND URBAN DEVELOPMENT

24 CFR Part 3500

[Docket No. FR-5180-F-06]

RIN 2502-AI61

Real Estate Settlement Procedures Act (RESPA): Rule to Simplify and Improve the Process of Obtaining Mortgages and Reduce Consumer Settlement Costs; Withdrawal of Revised Definition of "Required Use"

AGENCY: Office of the Assistant Secretary for Housing-Federal Housing Commissioner, HUD.

ACTION: Final rule.

SUMMARY: This final rule withdraws the revisions to the definition of "required use" as provided in HUD's November 17, 2008, final rule amending its Real Estate Settlement Procedures Act (RESPA) regulations. The November 17, 2008, final rule, in part, revised the existing definition of "required use," for the purpose of enhancing protections for consumers from deceptive mortgage practices that result from certain affiliated business transactions. The revised definition of "required use" had been scheduled to become effective on January 16, 2009. On January 15, 2009, and March 10, 2009, HUD published final rules delaying the effective date of the definition of "required use." The March 10, 2009, final rule provides for an effective date of July 16, 2009. The March 10, 2009, rule also solicited comment on whether HUD should withdraw the revised definition of "required use" and, if so, whether HUD should initiate new rulemaking on the subject. HUD has taken into consideration the public comments received and has decided to withdraw the revised "required use" definition. HUD therefore leaves in place the definition of "required use" before the revisions made by the November 17, 2008, final rule.

HUD remains committed to the RESPA reform goals of the November 17, 2008, final rule and concerned about some of the practices reported by commenters, and will initiate a new rulemaking process on required use.

DATES: Effective Date: **[Insert date 30 days after date of publication in the FEDERAL REGISTER**.], except that the amendment to 24 CFR 3500.2 is effective July 16, 2009.

FOR FURTHER INFORMATION CONTACT: Ivy Jackson, Director, or Barton Shapiro, Deputy Director, Office of RESPA and Interstate Land Sales, Office of Housing, Department of Housing and Urban Development, 451 7th Street, SW, Room 9158, Washington, DC 20410-8000; telephone 202-708-0502 (this is not a toll-free telephone number). Persons with hearing or speech impairments may access this number through TTY by calling the toll-free Federal Information Relay Service at 800-877-8339.

SUPPLEMENTARY INFORMATION:

I. Background

On November 17, 2008 (73 FR 68204), HUD published a final rule amending its regulations in 24 CFR part 3500 to further the purposes of the Real Estate Settlement Procedures Act of 1974 (12 U.S.C. 2601-2617) by requiring more timely and effective disclosures related to mortgage settlement costs for federally related mortgage loans to consumers. The final rule followed publication of a March 14, 2008, proposed rule (73 FR 14030) and made changes in response to public comment and further consideration of certain issues by HUD. Additional information regarding the RESPA regulatory amendments, and specifically changes made by HUD subsequent to the proposed rule, is provided in the preamble to the November 17, 2008, final rule.

The November 17, 2008, final rule became effective on January 16, 2009, but provided a longer transition period for the majority of the new requirements. Other provisions, however, were scheduled to become applicable on January 16, 2009. Among regulatory changes identified as being applicable upon the effective date of January 16, 2009, is the revised definition of the term "required use." The revision of that definition became the subject of litigation, following issuance of the final rule. (See National Association of Home Builders, et al. v. Shaun Donovan, et al., Civ. Action No. 08-CV-1324, United States District Court for the Eastern District of Virginia, Alexandria Division.)

HUD issued a final rule on January 15, 2009 (74 FR 2369) that deferred the effective date of the revised definition of "required use" for an additional 90 days until April 16, 2009. On March 10, 2009 (74 FR 10172), HUD published a final rule further delaying the applicability date of the revised definition of "required use" until July 16, 2009. The effective and applicability dates of the remaining provisions of the November 17, 2008, final rule were not affected by the January 15, 2009, and March 10, 2009, final rules, and they are not affected by this final rule.

During this time HUD reviewed the provisions on "required use" and, through the March 10, 2009, rule also solicited public comment on whether HUD should withdraw the definition, as promulgated in the November 17, 2008, final rule, for the purpose of further evaluating the scope and operation of the required use provision, and on initiating new rulemaking.

II. This Final Rule - Withdrawal of the Definition of "Required Use"

This final rule withdraws the revisions to the definition of "required use" made by HUD's November 17, 2008, final rule, and leaves in place the definition codified in the RESPA regulations at 24 CFR 3500.2 prior to that revision.[1] HUD remains committed to the goals of RESPA reform and concerned about affiliated business practices that interfere with consumer choice. Therefore, HUD will initiate new rulemaking to address RESPA's prohibitions on required uses.

The proposal to withdraw the "required use" definition was of significant public interest. HUD received over 1,200 comments in response to the solicitation of public comments. The comments were highly informative and highlighted, among other things, the potential complexity of the affiliated business requirements and the need for further clarity on the application of "required use". The comments also underscored the need for HUD to continue to pursue reform in this area.

Based upon HUD's further evaluation of affiliated business arrangements, and HUD's review of the comments, HUD determined that its revised definition of "required use" did not strike the right balance between HUD's goals of enhancing consumer protection consistent with the statutory scheme of RESPA and providing needed guidance to industry participants. Through this final rule, HUD is therefore withdrawing the revised definition of "required use," and leaving in place the definition currently codified in 24 CFR 3500.2. It is HUD's view that, especially given the attention focused on HUD's concerns through this rulemaking, the prior

[1] Note that the definition of "required use" in the November 17, 2008, final rule did not take effect on January 16, 2009, and has not taken effect. As a result, the definition of "required use" currently codified in HUD's RESPA regulations at 24 CFR 3500.2 has remained the applicable definition pending the revised definition's effective date. With HUD's withdrawal of the definition set forth in the November 17, 2008, final rule, the codified definition continues to be the applicable one.

definition of "required use" can be used to address some deceptive referral arrangements, even though it does not achieve the enhanced consumer protections that HUD sought with respect to mortgages involving affiliated business arrangements. HUD will continue to seek consumer protections, especially as mortgage products continue to change, often becoming more complex and challenging buyers' understanding of the costs and nature of mortgage transactions. HUD is not abandoning its goal of providing greater protections to consumers in real estate settlement transactions, but remains open to different means of achieving this goal.

New rulemaking offers HUD the opportunity to present a new proposal based upon its reevaluation of the required use provision in the affiliated business contexts, including the development of analysis in support of a new proposal, as well as applied in its various contexts in the RESPA regulations, and as further informed by the public comments received on the March 10, 2009, rule. New rulemaking will allow HUD to further refine its regulations on practices that are prohibited under other RESPA provisions. At the same time, HUD believes better success will be achieved by providing consumers, industry, and other interested members of the public the further opportunity for input into this area of RESPA reform.

III. Discussion of the Public Comments Received on the March 10, 2009, Final Rule

The public comment period on the March 10, 2009, rule closed on April 9, 2009. HUD received over 1,200 comments on withdrawal of the revised definition of "required use". Comments were submitted by mortgage servicers, homebuilding companies, builder-affiliated mortgage and settlement service providers, real estate and mortgage professional associations, and consumers. Many of the comments were form letters from members of industry organizations, with multiple commenters registering nearly identical comments and concerns.

The March 10, 2009, rule sought comments on the withdrawal or non-withdrawal of the revised definition of "required use". Some comments submitted in response to the March 19, 2009, final rule addressed other aspects of RESPA, however; for example, suggesting other changes to HUD's RESPA regulations or disclosure forms. Comments submitted on other aspects of the November 17, 2008, final rule, or RESPA reform, are outside the scope of the March 10, 2009, rulemaking and are not addressed in this final rule.

The summary of comments that follows presents the major issues and questions raised by the public commenters on the withdrawal of the revised definition of "required use". The summary is organized in two sections. The first section summarizes the comments opposed to withdrawal of the required use revision, and the second section summarizes those comments supporting withdrawal. Due to the similarity and overlap of the issues raised by commenters, HUD has provided a consolidated response at the end of the description of the public comments.

A. Comments Opposed to Withdrawal of Required Use Definition

Comment: Revised "required use" provision is needed to promote competition. Of those commenters opposing withdrawal, the overwhelming basis cited is the absence of needed competition that would result if the revised definition of "required use" were withdrawn. The commenters wrote that homebuilders have established a system that restricts buyers to the use of mortgage lenders owned by or affiliated with the builders, thereby eliminating the choices available to consumers. Commenters stated that this practice of linking incentives to the use of certain lenders discourages consumers from shopping for service providers and, since closing is some time in the future, the buyer cannot determine at the time of application whether the interest rate of the mortgage offered in exchange for the incentive will be competitive. Commenters stated that the cost of giving up the incentives agreed to at the time of application

may be too great for a buyer to bear even though the loan rate at the time it is locked turns out to be unfavorable. Commenters wrote that often buyers do not have sufficient knowledge to select an appropriate lender and are at the mercy of the builder; that buyers are not skilled enough in real estate transactions to realize they are being taken advantage of.

The commenters wrote that the revised definition of "required use" in the November 17, 2008, final rule would preclude these practices and promote competition beneficial to homebuyers. The commenters wrote that while, on their face, the incentives are worth many thousands of dollars, they are actually priced into the cost of the home and permit the lender to charge higher rates or fees. The commenters stated that often the incentives are recouped in the home sales price or the loan rate without disclosing it to the consumer, with the result that consumers have been overpaying for homes and mortgages without realizing it. The commenters stated that the rates offered by the builder-affiliated lender are typically significantly higher than what the borrower would obtain from free market shopping.

The commenters opposing withdrawal wrote that if builder-affiliated lenders were really offering competitive terms, they would not need to offer incentives that "force" the client to the affiliated lender. The commenters also wrote that the purpose of RESPA is to protect the public and allow them to shop for the best services and prices. The commenters stated that a delay in implementation of the required use provision would defeat this statutory purpose.

Comment: The revised "required use" definition is needed to prevent conflict of interest and similar abuses. Several commenters wrote that allowing required services in exchange for incentives not only excludes competition, but results in borrowers signing with certain lenders, even though other lenders offer lower rates, which is a practice that is unethical, "collusion," anti-competitive," and ripe for abuse and fraud. The commenters wrote that it is a conflict of

interest to have a builder-owned mortgage company financing the builders' own homes, and for an incentive offered by a builder to require a borrower to use a certain lender. The commenters stated that often the builder is not actually providing the consumer with a discount because the cost of the incentives is buried in the loan rate or the cost of the home. The commenters wrote that the unethical features of this arrangement are underscored by the fact that the builder does not disclose to the buyer until closing that the use of a specific, higher-rate lender is required. The commenters stated that the disclosure is sometimes buried in unclear contract language. The commenters stated that this practice has resulted in borrowers getting loans with higher rates, resulting in greater numbers of foreclosures.

Comment: The practice of linking builder incentives to the use of an affiliated mortgage company is unfair to other lenders. The commenters stated that even if buyers would prefer another lender, once they are presented with an incentive, they feel they must use the builder's "joint venture" lender or the incentive will be withdrawn. Several lenders commented that they often lose business to other lenders because of these incentives. Commenters stated that the tradeoff is unfair both to buyers because of the higher loan costs and to lenders who cannot compete with the builder's arrangement. Another commenter wrote that builder-affiliated lenders typically employ marginal loan officers that are merely order-takers and do not possess the education, experience, or knowledge to competently evaluate a potential borrower's financial situation, further jeopardizing the opportunity for consumers to choose a beneficial mortgage product.

The commenters stated that buyers should be able to keep the incentives and also choose their lender. One commenter wrote that these incentives are an "injustice" and a "restraint of trade." Other commenters stated that builders are in control of every aspect of the transaction

and are using these incentives simply to make more money, without actually providing a benefit to consumers contrary to advertisement. Commenters urged HUD to make home buying a fair playing field for consumers and lenders, and force builders to follow the same rules that other parties to the real estate transaction must follow.

B. Comments Supportive of Withdrawal of Revised Definition of "Required Use"

Comment: The revised required use provision would destroy homebuilder-affiliate business model and corresponding builder forward commitments. Many commenters wrote that the required use provision would unnecessarily destroy the homebuilder-affiliate business model, driving many builder-affiliated lenders out of business. The commenters wrote that one of the incentives most frequently offered is the buying down of interest rates through the purchase of forward commitments. In exchange for a fee, the homebuilder buys down the interest rates in the commitments to present attractive financing to their customers. Because commitments are expensive and require that a significant number of the homebuilder's customers use the lender, homebuilders limit the companies they purchase commitments from to their affiliates. The commenters wrote that the revised required use provision would prohibit homebuilders from purchasing forward commitments from affiliates, but would not prohibit these arrangements with unaffiliated lenders. In consequence, the final rule would terminate the ability of builders to help consumers obtain competitively priced credit.

In a similar vein, commenters stated that the revised required use provision would preclude homebuilders from offering other incentives to customers who use affiliated lenders – such as closing cost credits and home upgrades – unless homebuilders offer the incentives regardless of the settlement service provider. The commenters wrote that the joint business model depends on the ability to offer incentives to encourage the use of affiliates. According to

the commenters, many affiliated lenders do not otherwise advertise or market their products to the general public. The commenters wrote that affiliated lenders who are not designed to compete on the open market would lose considerable business as a result of the revised required use provision.

Comment: The revised definition of "required use" creates an unintended loophole that decreases rather than increases consumer protections. Some commenters stated that the revised definition of "required use" is worded in a confusing way that provides builders with a "loophole" that would decrease, rather than increase, consumer protections and competition. This loophole, according to a commenter, allows builders to set up their own mortgage company and offer incentives through that company, and thereby escape the oversight and protections sought by HUD's revised definition of "required use". Commenters wrote that a definition of "required use" should clearly state that borrowers are allowed to shop for settlement services free of any influence from the builder and that incentives should be offered regardless of the customer's choice for mortgage or title services.

Other commenters wrote that HUD failed to analyze the potential impact of the new definition of "required use" and that the revised definition engenders a more confusing, less transparent loan origination process that will discourage consumer free choice. Commenters urged HUD to draft a more narrowly focused definition that would not prohibit builders, real estate brokers and others from offering genuine incentives to customers. The commenters stated their support for withdrawal of the revised definition of "required use" but also stated their support for HUD to continue to pursue reform in this area.

Comment: The revised definition of "required use" lacks the necessary foundational support for the change to the definition of "required use". Some commenters wrote that the

revised definition of "required use" is based solely on anecdotal evidence, and not supportable data. The commenters disagreed with HUD's statements that homebuilder-affiliated lenders may not offer the best products and services, that their fees may be higher than their competitors, and that the transactions are too complicated for borrowers to calculate the value of the package deal they receive when using an affiliated lender. The commenters wrote that the justifications offered by HUD were "incomplete, confusing, inaccurate, and /or based upon flawed reasoning or suspect evidence."

Definition of "required" is contrary to the term's plain meaning under RESPA. Some commenters wrote that the revised definition of "required use" is contrary to the plain meaning of the words in the RESPA statute itself because defining "required use" to mean any incentive offered to a buyer to use an affiliated company contradicts the unambiguous meaning of the statutory term "required." The commenters wrote that HUD should not confuse legitimate incentive arrangements with undue influence of required use of a product or service. The commenters also wrote that the required use provision contradicts the mandate of Section 8(c) of RESPA that the only criteria that may be imposed on affiliated business arrangements are those contained in the statute**.**

The revised definition of "required use" is beyond the scope of HUD's authority. Some commenters wrote that HUD should withdraw the definition of "required use" because the revised definition is beyond the scope of HUD's authority under RESPA. The commenters wrote that RESPA prohibits agency restrictions on affiliated business associations except those contained in the statute itself. The commenters wrote that HUD's rulemaking authority extends only to interpret RESPA, to implement the statute, and to grant exemptions that broaden the permissibility of certain behavior. According to the commenters, Congress did not give HUD

the power to prescribe additional restrictions, which HUD did in its revision to the definition of "required use," and therefore the revised definition is invalid. The commenters wrote that RESPA prohibits any limitation on affiliated business association other than requiring that a proper disclosure is given, the person is not required to use a particular settlement service provider, and nothing of value is received other than payments permitted under RESPA. The commenters wrote that RESPA demonstrates that Congress intended to favor affiliated business arrangements in nearly every manifestation**.**

Comment: Revised required use provision unfairly targets homebuilders. Several commenters objected to the required use provision on the basis that it unfairly singles out homebuilders from all other entities involved in the sale and financing of real estate. The commenters wrote that the rule would not prohibit lenders from offering incentives to homebuyers who use an affiliated title company. Similarly, the commenters stated, real estate agents would be able to offer incentives to homebuyers that use the agent's affiliated lender or title company. The commenters wrote that consumers should not be denied access to the legitimate incentives offered by builder-affiliated lenders because of a few unscrupulous lenders and builders. The commenters wrote that there is no rational basis to support the proposition that homebuilders should be treated differently from other entities.

Comment: Builder affiliated lender model has efficiencies which are passed on to consumers. Commenters supporting withdrawal stated that affiliated lenders can assist and create efficiencies that result in discounts in a complex transaction that non-affiliated lenders cannot always handle in a timely manner because of their lack of experience with new home sales. These commenters emphasized the convenience of "one stop shopping" as a significant consumer benefit that will be eliminated unless HUD withdraws the revised definition of

"required use." The commenters wrote that rather than a consumer having to deal with multiple settlement service providers, affiliated providers coordinate the home purchase process by finding a loan which they underwrite and ensure that the funding will be ready at the closing date selected by the builder and buyer. The commenters wrote that consumers receive better service from affiliated lenders because of the efficiencies resulting from the relationship with the builder, the linked communication systems and standardized policies, and the lender's own desire to obtain repeat business and recommendations. Because affiliated lenders work with high volumes of transactions, they have proven controls that ensure a complete, fast, and fair transaction. Affiliated lender commenters wrote that because of their affiliation, they have been able to help borrowers who have had problems with other lenders or who needed to close quickly. The commenters wrote that post-closing surveys show a customer satisfaction rate of 90 percent with affiliates.

Comment: Affiliated companies help prevent mortgage fraud. Commenters wrote that when outside lenders are involved, the potential for mortgage fraud is greater than when consumers use affiliated companies because the outside lender's personnel are often not as well trained as the personnel of affiliated lenders. Commenters stated that because of their lack of affiliation, outside lenders do not have as great a motivation to prevent fraud as do affiliated lenders. The commenters stated that in affiliated relationships, both entities can work together to prevent mortgage fraud.

C. HUD Response to the Public Comments

HUD appreciates all the comments submitted in response to the solicitation of comment in the March 10, 2009, rule, on the proposal to withdraw the revised "required use" definition in the November 17, 2008, final rule. HUD reviewed and gave careful consideration to all views

expressed. Following consideration of the comments and HUD's further evaluation of the definition and application of "required use" HUD has decided to withdraw the revised definition and, leave in place the definition of "required use" as found in HUD's codified regulations in 24 CFR 3500.2, and which has remained in effect since the revised definition of "required use" in the November 17, 2008, final rule, had not taken effect.

HUD reiterates its commitment to fair real estate settlement practices that are not misleading, prevent abuse, offer proper disclosures to homebuyers, and promote choice and competition. HUD's intent in revising the definition of "required use" was to clarify its interpretation of RESPA's requirements with respect to transactions involving affiliated businesses in order to promote more competition among settlement service providers. After further evaluation and consideration of the concerns voiced by consumers and industry participants from various fields about the application of the revised definition of "required use," HUD has concluded that all would benefit by HUD withdrawing the revised definition and addressing "required use" through new rulemaking.

HUD recognizes that the affiliations of businesses involved in complex home purchase transactions can themselves be complex arrangements, and that consumers may have difficulty understanding whether there is value in using affiliated businesses in mortgage transactions. HUD has determined that further development of the concept of "required use" is necessary to assure that, especially in the affiliated business context, its application protects consumers by eliminating abusive practices that increase costs for unsuspecting consumers. The comments submitted in response to the March 10, 2009, rule provide HUD with a good starting point for going forward on this issue. Consumers and industry and the public generally will have further opportunity to offer feedback when HUD issues a new proposed rule on this subject.

Although HUD is withdrawing the revised definition of "required use," a definition of "required use" remains part of HUD's RESPA regulations. That definition, which focuses its discount language on settlement services, is the one that was in place in HUD's RESPA regulations prior to HUD's issuance of the November 17, 2008, final rule, and which has remained in place since the revised definition of "required use" never took effect. Additionally, although HUD is withdrawing the revised definition of "required use", the withdrawal should not be interpreted to signal any lessening of HUD oversight or enforcement of existing statutory and regulatory provisions in this area. HUD interprets its definition generally as aiming to distinguish the features of legitimate incentives and discounts offered to consumers from those that may result in undisclosed or higher costs to consumers. The public comments on this subject underscore the need for greater attention to and understanding of the treatment of discounts to consumers under RESPA and HUD's RESPA regulations.

With respect to the more specific issues expressed by commenters on the subject of "required use", HUD will defer further discussion of such issues to any new rulemaking. Generally, however, HUD notes that it revised the definition of "required use" to more effectively realize Congress's intent in passing RESPA. RESPA's principal goal is consumer protection. RESPA provides HUD with the requisite authority to promulgate a revised definition of "required use" that meets the goals of RESPA and HUD's mandate to enforce RESPA. Today's final rule will enable HUD to reconsider all of the issues involved in the application of the required use concept and to better craft requirements and limitations that address the valid concerns raised in the preceding rulemaking.

IV. Findings and Certifications

Federalism Impact

This rule does not have federalism implications and does not impose substantial direct compliance costs on state and local governments or preempt State law within the meaning of Executive Order 13132 (entitled "Federalism").

Unfunded Mandates Reform Act

Title II of the Unfunded Mandates Reform Act of 1995 (2 U.S.C. 1531-1538) (UMRA) requires federal agencies to assess the effects of their regulatory actions on state, local, and tribal governments and on the private sector. This rule does not, within the meaning of the UMRA, impose any federal mandates on any state, local, or tribal governments nor on the private sector.

List of Subjects in 24 CFR Part 3500

Consumer protection, Condominiums, Housing, Mortgagees, Mortgage servicing, Reporting and Recordkeeping requirements.

Accordingly, 24 CFR part 3500 is amended as follows:

PART 3500—REAL ESTATE SETTLEMENT PROCEDURES ACT

1. The authority citation for part 3500 continues to read as follows:

Authority: 12 U.S.C. 2601 et. seq: 42 U.S.C. 3535(d).

2. Section 3500.1(b)(1) is revised to read as follows:

§ 3500.1 Designation and applicability.

* * * * *

(b) * * *

(1) Sections 3500.8(b), 3500.17, 3500.21, 3500.22 and 3500.23, and Appendices E and MS-1 are applicable commencing January 16, 2009.

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3. In § 3500.2, revise the definition of "Required use" to read as follows:

§ 3500.2 Definitions.

* * * * *

Required use means a situation in which a person must use a particular provider of a settlement service in order to have access to some distinct service or property, and the person will pay for the settlement service of the particular provider or will pay a charge attributable, in whole or in part, to the settlement service. However, the offering of a package (or combination of settlement services) or the offering of discounts or rebates to consumers for the purchase of multiple settlement services does not constitute a required use. Any package or discount must be optional to the purchaser. The discount must be a true discount below the prices that are otherwise generally available, and must not be made up by higher costs elsewhere in the settlement process.

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Dated: May 7, 2009

Ronald Y. Spraker
Acting General Deputy Assistant Secretary for Housing-
Deputy Federal Housing Commissioner

[FR-5180-F-06]