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### **RESPA, the Good Faith Estimate, and the HUD-1 Form**

When borrowers are looking at taking out a massive loan to finance the purchase of a new house, the closing costs (also known as "settlement costs") may seem like small change. These costs can add up to around four or five percent of the total cost of the house, however, which is not an insignificant amount of money. It is very important that borrowers make sure that they are receiving the most competitive arrangement possible for the settlement costs that come along with closing on a house, or they could end up paying much more than they had expected.

Fortunately, there are laws and regulations that require lenders to disclose certain information about closing costs, including a "good faith estimate" of the total costs. These disclosures can help borrowers verify that they are getting the best deal possible. New rules can even result in refunds to borrowers if the lender's good faith estimate is too far below the actual closing costs.

The law that gives rise to the rules surrounding settlement costs is known as the Real Estate Settlement Procedures Act, or RESPA. This article will briefly explain a few of RESPA's provisions and how they relate to settlement costs and procedures.

#### **What Are Settlement Costs?**

The terms settlement costs and closing costs are interchangeable and refer to the fees, taxes, and payments required to settle a real estate transaction. Since real estate transactions are quite complex, there can be a long list of associated costs. Typical items that make up the settlement costs include:

- Legal fees
- Title searches and examinations
- Title insurance
- Recording fees
- Notary services
- Pest and house inspections
- Document preparation services
- Taxes
- Surveys

#### **How Does RESPA Affect the Settlement Process?**

RESPA is a very important consumer protection statute. It does not govern the amount of the costs, but it does ensure that consumers receive accurate information about what costs they can expect for their real estate deal. While RESPA has many provisions, the two of particular interest here concern disclosures to borrowers and prohibitions on lenders.

The specific disclosure that relates to settlement costs involves a lender's good faith estimate of the total amount of the settlement costs. New rules issued under RESPA require lenders to issue this good faith estimate within three days of receiving a loan application. Note that this requirement is met if the lender puts the GFE in the mail within three days; the borrower may receive it later than that.

RESPA also prohibits certain practices by lenders that can drive up closing costs, such as accepting kickbacks for referring mortgage settlement business or requiring borrowers to purchase title insurance from a certain provider.

#### **What's the Point of a Good Faith Estimate?**

The good faith estimate, or GFE, that borrowers receive from lenders provides important information that borrowers can use to make sure that they are receiving the best deal on the purchase of their home. By requesting GFEs from several

different companies, borrowers can compare estimates and select the lender who offers the lowest costs.

It is important to stop here and note the difference between an informal worksheet estimate and a GFE. Mortgage providers will often use a worksheet to provide a borrower with a rough estimate of the likely closing costs, which the borrower can use as they are comparing lenders. The use of these worksheets is perfectly legitimate; however, they are not guaranteed by RESPA. A formal GFE, on the other hand, is guaranteed and subject to certain requirements. Most importantly, for the vast majority of single-family home loans, a GFE must not underestimate the closing costs by more than a specified amount, known as the "tolerance level." If the good faith estimate is too low, the lender may have to provide a refund to the borrower to cover the discrepancy.

Lenders must provide a GFE upon request, and cannot require applicants to commit to the company before issuing a GFE.

### **What's a HUD-1 Form?**

The HUD-1 form adds up the actual costs of a closing (as opposed to the good faith estimate, which lists the *estimated* costs.) The settlement agent for the transaction will prepare one, and a borrower is entitled to view the HUD-1 form 24 hours before the actual settlement.

Each settlement cost will appear on the HUD-1 form as a separate item to make it easier for borrowers to understand what they're paying for. Borrowers can compare the items and amounts on the HUD-1 form with the good faith estimate they received from their lender to see if there is any difference. As mentioned above, if there is a difference between the GFE and the HUD-1 and that difference exceeds the tolerance levels, borrowers may be eligible for a refund from their lender.

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