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In-Depth Reports

Be careful of what you ask for

A war is still raging over whether affiliated business arrangements are a device of the devil or not. Independent title agents, who, like cattle herders, gather their customers from the four corners of the earth, detest captive developer title agents who, like sheep herders, see their flock devour every customer in a development.

The Department of Housing and Urban Development (HUD) entered the war on the side of the independent title agents when it outlawed builder incentives tied to the use of affiliated or favored title agents and mortgage brokers. Builders fought back in court, forcing HUD to reverse its definition of "required use" of a settlement service provider. I commented on HUD's definition in a [prior column](#), pointing out some of the loopholes in the new definition of "required use."

However, setbacks rarely mean defeat. HUD published an Advance Notice of Proposed Rulemaking (ANPR) to gather evidence that changing the definition of required use is justified as a way to reduce consumer costs. In a somewhat rhetorical fashion, HUD asks whether builder incentives given to buyers are actually baked into the price of the home and are not true incentives for the use of an affiliated or favored business. HUD also asks, somewhat theoretically, whether forward commitments purchased by builders are proper under RESPA.



HUD's ANPR mentions "builder" 23 times while no other incentive monger is mentioned even once. This does not mean that a definition of required use promulgated by HUD will not have any impact on other affiliated businesses. If a builder is prohibited from giving the borrower a pool or paying for the closing to induce the borrower to use the affiliate's services, why should a bank be allowed to give its affiliated mortgage company a warehouse line of credit? After all, there is no difference, in theory, between the bank providing the money to close the loan at its affiliate and the builder paying for the closing at its affiliate. The borrower is getting something of value either way that is baked into the cost of the transaction.

There are, of course, other companies that provide incentives to use an affiliated title agency. Title agents that provide group unemployment insurance to borrowers are buying the policy from an affiliated insurance agency. Mortgage companies that give the consumer a TV at closing are buying the TVs from an affiliated or preferred appliance store. It is rumored that Amway previously provided its goods to consumers who obtained a loan from an affiliated mortgage company, with HUD's blessing.

When we consider that HUD might restrict forward commitments, the potential impact of the rule that follows the ANPR becomes even greater. Forward commitments are integral to secondary market transactions. If HUD intends to restrict forward commitments, it can only do this effectively by eliminating the secondary market exception and requiring disclosure of all lender income on the Good Faith Estimate and HUD-1 Settlement Statement. The impact of disclosing secondary market income as a tolerance restricted origination fee will be enormous. Every loan will be hedged to lock in income levels to avoid a RESPA violation. And, if you thought that the new HUD-1 made Truth in Lending Act compliance difficult,

wait until you throw loan sale income into the GFE block 1/HUD line 801 melting pot.

Will HUD have the foresight to draft a rule that avoids the foibles of unintended consequences? It seems a Herculean task to draft a rule that addresses "builders" without impacting other portions of the industry. A rule that is expressly targeted at builder joint ventures is subject to attack as arbitrary and unauthorized by RESPA. A rule that is too broad could increase costs across the board for consumers. Is there a happy medium, or should we expect another round of pandemonium?

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