

Understanding the Good Faith Estimate

Pursuant to the provisions contained in the Real Estate Settlement Procedures Act and Section 3500.7 of Regulation X, a mortgage lender or mortgage broker must provide a Good Faith Estimate of Settlement Charges to a borrower within three days of the date that the lender or broker receives or prepares the Good Faith Estimate (sometimes referred to as a “GFE”).

The Good Faith Estimate (GFE) must provide an estimate of the amount of any settlement services a borrower is likely to incur in connection with the transaction to which the application relates. The estimate of the charges can be provided as a range of amounts.

Regulation X also provides a suggested form to be used for this purpose and although not mandatory the vast majority of lenders provide Good Faith Estimates in a form similar to that set forth in the regulation which also corresponds with the form of the HUD1 Settlement Statement that will be used at the closing of the transaction. An applicant that receives a GFE in the suggested form can therefore more easily compare the estimated charges that were provided at the time application with the final charges shown on the settlement statement.

The suggested form lists the charges in six (6) sections of numbered lines and although the specific verbiage for many or most of the fees may vary from lender to lender the format of dividing the fees into six (6) sections is utilized by the vast majority of lenders providing the form.

The “800” Section

The first section is referred to as the “800” Section and includes “Items Payable in Connection with the Loan”. These are the fees paid to the mortgage brokers and lenders in connection with the transaction. An origination fee is commonly set forth on Line 801, discount points paid by the borrower are set forth on Line 802, and the appraisal and credit report fees are set forth on Lines 803 and 804 respectively. The remainder of the fees paid to the mortgage brokers and lenders will be set forth on the remainder of the lines in the “800” section of the GFE. The nomenclature used to describe these various fees is as diverse as it is irrelevant. Semantics are unimportant. The borrower should merely be concerned with the cumulative amount of the fees contained in this section as that cumulative total will be the only figure a borrower needs to compare rate and pricing quotes from competing lenders.

Near the end of the “800” Section of the GFE there may be a line indicating the amount of the Yield Spread Premium (or “YSP”) paid “POC” to the Mortgage Broker by a Wholesale Mortgage Lender that table funds the transaction.

800	Items Payable in Connection with Loan	
801	Origination Fee (1.000%)	\$2,000.00
802	Discount Fee (0.500%)	\$1,000.00
803	Appraisal Fee paid to XY Z Mortgage	\$325.00
804	Credit Report Fee paid to XYZ Mortgage	\$18.00
805	Underwriting Fee pd to ABC Wholesale Mortgage Co	\$450.00
806	Tax Service Fee paid to ABC Wholesale Mortgage Co	\$70.00
807	Flood Certification Fee pd to ABC Wholesale	\$10.00
808	Processing Fee pd to XYZ Mortgage	\$200.00
809	Courier Fee pd to XYZ Mortgage	\$50.00
810	Yield Spread Premium (\$1,000) pd POC to XYZ by ABC	

This yield spread premium (which may also be described a countless number of different ways) is compensation paid to the loan originator by a wholesale mortgage source that table funds the transaction. Just because the premium is not listed on the HUD1 form does not mean it does not exist. Originators that fund their loans in an alternate manner (through use of temporary bank “warehouse” funding) are not currently required by law to disclose the amount of the premium on either the GFE or the HUD1 settlement statement even though they are receiving the premium in the same manner as the mortgage broker. There is a great deal of “hoopla” in Washington relating to the “premium” and whether and how it should be disclosed to consumers. Quite frankly, a consumer should have not interest in the fee whatsoever since the borrower is not paying the fee. Who cares what compensation the lenders are receiving in the transaction? The borrower should only be concerned with the charges he is required to pay and how the cumulative amount of those charges compare the charges of the lender’s competitors for the identical loan program at the identical rate of interest. The YSP is irrelevant in making this determination.

The “900” Section

The next Section of the GFE is the “900” Section which includes “Items Required by the Lender to be paid in Advance”.

Line 901 will typically set forth the “prepaid interest” that is paid by the borrower on the new loan from the date of closing through the last day of the month.

900	Items Required by the Lender to be Paid in Advance	
901	Prepaid Interest from 3/28/07 to 4/1/07 @ \$23.00 per day	\$92.00
902	Mortgage Insurance Premium paid to MGIC	\$1,000.00
903	Hazard Insurance Premium paid to QRS Casualty Co	\$1,150.00
904		

Why does a borrower pay “prepaid interest”? Most mortgage notes will be drawn in a manner such the borrower will be required to make a monthly installment payment on the 1st day of each month. In the vast majority of cases the first payment on a mortgage loan will be due on the 1st day of the second month following the date of closing. For example, if a transaction closes in the March on the 28th the first payment will be due on the 1st day of May (34 days after the closing date). Most notes are prepared so that the principal amount is paid in equal payments that are computed so that the loan will fully amortize over a specific term (e.g. 360 months [30 years]). To amortize correctly each payment includes a portion that is used to pay exactly one month of accrued interest. Thus in our example the payment made on May 1st will include a payment equal to 30 days of interest that accrued during the month of April. But what about the other 4 days of interest to which the lender is entitled for the period from the date of closing through the final day of the month (4 days in our example). The lender is compensated for these odd days of interest by payment in advance at closing. And that my friends, is the “prepaid interest”. In some cases when the loan closes during the first few days of the month the lender will permit a “short pay”. A “short pay” describes the situation when a lender will arrange to draw the note so that the payment is due on the 1st day of the month *following* the month in which the closing occurred. Thus, if the loan closed on the April 4th the normal rule would be to have the first payment due on June 1st (in the *second* month following the date of closing). With a “short pay” the lender will draft the note so that the first payment is due on May 1st. This is done so the borrower does not have to bring something close to a full month of interest to closing. Borrowers with limited cash for closing might have trouble coming up with a full month of interest to be paid in advance.

Because the note is drawn so that the borrower has to make the full amount of the payment (that would typically include 30 days of earned interest) the lender will be collecting 3 days of interest in first payment that was unearned (from the 1st through the 3rd of April). To adjust for these few days of unearned

interest the borrower will typically be given a credit for those three days of unearned interest at closing (and this credit will appear on Line 901 as a negative amount) or the lender will refund those few days of unearned interest by a check or credit issue after closing.

If the borrower is required to pay for private mortgage insurance, an FHA mortgage insurance premium, or a VA Funding Fee any advance payments will be shown on Line 902.

Line 903 will set forth the amount of any prepaid hazard or casualty (homeowner's) insurance that the borrower is required to pay in advance. If insurance premiums will be escrowed and paid by the lender on the borrower behalf, the borrower will always be required to pay the premium for a full year of hazard insurance in advance. This is because insurance premiums are paid in advance.

Even if escrows are waived the vast majority of lenders will require the hazard insurance premium in a purchase transaction to be paid in advance for a full year. After the first year, the borrower that is paying taxes directly (rather than through an escrow/impound account managed by the lender) will then typically have the option to begin paying premiums quarterly or monthly.

In refinance transactions the borrower will only be required to pay a hazard insurance premium at closing when the renewal date for the borrower's existing policy falls within the date of closing and a date that is less than 30 days (and sometimes 60 days) after the date of closing. Because a lender does not want a lapse of insurance coverage on the property given as collateral to secure the loan it will require that the premiums that are due before or within a month after closing be paid to assure that the lapse in coverage will not occur. If the renewal date is more than a month or two after closing the borrower will not be required to pay any advance premiums on Line 903 in refinance transactions.

The "1000" Section

The "1000" Section of the GFE includes "Reserves Deposited with Lender". This is the section where the deposits made by the borrower to an escrow account (sometimes referred to as an "impound" account) maintained by the

1000	Reserves Deposited with Lender	
1001	Hazard insurance – 2 months @ \$90.00	\$180.00
1002	Mortgage Insurance – 0 months @ \$42.07	\$0.00
1003	City property taxes – 4 months @ \$102.00	\$408.00
1004	County property taxes – 4 months @ \$50.00	\$200.00
1005	ISD property taxes – 4 months @ \$901.00	\$3,604.00
1006	Assessments - months @ \$0.00	\$70.00
1007		\$10.00
1008		\$200.00
1009		\$50.00
1010	Aggregate adjustment	(\$90.00)

lender for the payment of taxes and insurance premiums on the property securing the loan will be listed.

If an borrower chooses or is required to "escrow" taxes and insurance premiums the lender will require the borrower to deposit to the escrow account at the time of closing, an amount of cash that when combined with the payments to escrow that will be made with each monthly principal and interest installment that will sufficient to pay the property taxes when due and the insurance premiums at renewal. The lender is also authorized by law to collect an amount equal to 1/6th (two months) of the annual amount of taxes and insurance premiums paid from the escrow account.

Thus, if the first payment date is on May 1st and taxes are paid in December of each year the borrower will make eight (8) deposits for taxes to the escrow account with each payment paid between May 1st and December 1st (8 payments). The lender is entitled to have 14 months of taxes in escrow in December

when the taxes are paid. For this reason the borrower will be required to deposit six (6) months of taxes at closing so that the lender will have 14 months in December prior to making the tax payment.

Similarly, if the insurance policy renews in September and the first payment date is May 1st the lender will receive five (5) monthly escrow deposits from the borrower between May and September. The lender is entitled to 14 months of insurance so the borrower will be required to deposit nine (9) months at the time of closing to insure that the lender will have an amount sufficient to pay the renewal premium and the two (2) month buffer permitted by law to account for any increases in the premium.

Each of the amounts deposited to the escrow account in this manner will listed in the “1000” Section of the GFE.

The “1100” Section

The “1100” Section includes “Title Charges”. This section will include the various fees and premiums paid to the escrow agent (settlement agent) and the title company in connection with the transaction.

Line 1101 will include the “settlement fee” (sometimes referred to as the “escrow fee” or “closing fee”) paid to the escrow agent (sometimes referred to as the “settlement agent”). This is a fee paid to the settlement agent for conducting the closing and handling the escrow in the transaction.

1100	Items Payable in Connection with Loan	
1101	Settlement or closing fee to Brazos County Title Co	\$250.00
1102	Abstract or title search to	\$0.00
1103	Title examination to	\$0.00
1104	Title insurance binder to	\$0.00
1105	Document preparation fee to Henderson Law Firm	\$150.00
1106	Notary fees to	\$0.00
1107	Attorney’s fees to	\$45.00
	<i>(includes above item numbers 1105)</i>	
1108	Title insurance premiums to Fidelity National Title Agency	\$0.00
	<i>(includes above item numbers 1102, 1103)</i>	
1109	Lender’s coverage \$160,000.00	\$100.00
1110	Owner’s coverage \$200,000.00	
1111	... Endorsements (T-36-\$25,\$0.00,T-17-\$25)	\$50.00
1112	... Tax amendments and NYDP	\$25.00

“Escrow” as used in this section is different than the “escrows” described in the “1000” Section of the GFE. Because the “escrow agent” is charged with the responsibility of collecting and disbursing the funds paid by the various parties into the agent’s escrow or “trust” account the fee charged for this service is often referred to as an “escrow” fee.

Lines 1102 through 1104 delineate fees paid to various participants in the title abstracting and examination process that are required for the issuance of a title insurance policy. In some regions of the country these services may be performed by different service providers. In other regions the title insurance company or its issuing agents will perform these functions. Thus, it is not uncommon for these lines to be left blank where the fee for these services is included as part of the premium paid for title insurance.

Line 1105 shows the estimated charge for preparing loan documents if the fee is paid to a party other than the lenders. Thus, in Texas, where attorneys are required to prepare or review the deed of trust, the fee paid to attorneys for this purpose are set forth at this line. A fee paid to a private document preparation company that is not associated or affiliated with the lenders might also appear on this line.

Line 1106 will show the fee paid directly to notary public for services performed in connection with a closing. Where the notary services are performed by the settlement agent or its employees this line might be blank as the notary services are included as part of the fee for services charged elsewhere in this section of the GFE.

Line 1107 will show the amount of any fees paid by the borrower to attorneys. The fees paid to attorneys for the preparation of loan documents will typically be listed at Line 1105. If an attorney is paid at closing for representing a party to the transaction or if a title attorney is paid for preparing other documents required at closing (such as releases or deeds) the fee paid to this attorney would likely be listed on this line.

Lines 1108 through 1113 will include the cumulative amount of all title insurance premiums (including charges for title insurance endorsements).

The “1200” Section

The “1200” Section includes “Government Recording and Transfer Charges”. This section includes the amount paid to the county clerk or registrar for recording deeds, deeds of trust, mortgages, releases of lien, transfers of lien, and affidavits. Fees paid for tax certificates and tax stamps will also be included in this section.

1200	Government Recording and Transfer Charges	
1201	Recording Fees to Brazos County Clerk	\$148.00
	<i>Deed: \$22.00 Mortgage: \$104.00 Releases: \$22.00</i>	
1202	City tax stamps: <i>Deed: \$0.00 Mortgage: \$0.00</i>	\$1,150.00
1203	County tax stamps: <i>Deed: \$0.00 Mortgage \$0.00</i>	
1204	Tax certificate to National Tax Research Corp	\$48.95

The “1300” Section

The “1300” Section is a “catch-all” section that includes other amounts charged in connection with the transaction, including fees paid to surveyors, property inspectors, contractors, and Homeowner’s Association of PUD dues and fees.

1300	Additional Settlement Charges	
1301	Survey to Metes N Bounds Surveyors	\$235.00
1302	Pest Inspection to Critters B Gone	\$48.00
1303	HOA Transfer Fee to Borger Heights HOA	\$25.00
1304	Home Service Warranty Contract to Home Protection Co	\$402.00
1305		
1306		

It is important to remember that the Good Faith Estimate does not create an obligation on the part of the mortgage brokers or lenders to provide services at the indicate amounts. It is merely an estimate and there is no express penalty for inaccurately estimating the charges. In most cases the mortgage brokers and lenders only control the fees contained in the “800” Section of the GFE and the Doc Prep fees paid at Line 1105. The remainder of the fees are controlled by and paid to third parties, most notably the title company and settlement agent.

To obligate a mortgage lender or broker to charge a specific amount in connection with a loan a borrower should secure a written agreement or commitment letter that specifically enumerates the charges that will be paid by the borrower in connection with the loan.