Consumer Financial Protection Bureau

CONSUMER FINANCIAL PROTECTION BUREAU FINALIZES "KNOW BEFORE YOU OWE" MORTGAGE FORMS

New Forms Improve Consumer Understanding, Aid Comparison Shopping, and Help Prevent Surprises

Washington, D.C. – The Consumer Financial Protection Bureau (CFPB) is issuing a rule today requiring easier-to-use mortgage disclosure forms that clearly lay out the terms of a mortgage for a homebuyer. The new "Know Before You Owe" mortgage forms will replace the existing federal disclosures and help consumers understand their options, choose the deal that's best for them, and avoid costly surprises at the closing table.

"Taking out a mortgage is one of the biggest financial decisions a consumer will ever make. Our new 'Know Before You Owe' mortgage forms improve consumer understanding, aid comparison shopping, and help prevent closing table surprises for consumers," said CFPB Director Richard Cordray. "Today's rule is an important step toward the consumer having greater control over the mortgage loan process."

For more than 30 years, federal law has generally required that within three business days after receiving a mortgage application, mortgage lenders must deliver two different, overlapping disclosures to consumers. At the closing stage, federal law again generally requires two forms. All of these forms contain duplicative and sometimes confusing information. The Dodd-Frank Wall Street Reform and Consumer Protection Act recognized the need to simplify and streamline this information for consumers and transferred responsibility for the forms to the CFPB.

Today's final rule requires that lenders use the CFPB's new disclosures, puts in place rules about when the new forms are given to the consumer, and limits how the final deal can change from the original loan estimate. The forms are available in English and Spanish.

- **The Loan Estimate:** This form will be provided to consumers within three business days after they submit a loan application. It replaces the early Truth in Lending statement and the Good Faith Estimate, and provides a summary of the key loan terms and estimated loan and closing costs. Consumers can use this new form to compare the costs and features of different loans.

- **The Closing Disclosure:** Consumers will receive this form three business days before closing on a loan. It replaces the final Truth in Lending statement and the HUD-1 settlement statement, and provides a detailed accounting of the transaction.

The CFPB conducted more than two years of extensive research, testing, and review to find out how to create mortgage disclosures that do what the law intended them to do: disclose information in a way that consumers can understand. A good disclosure helps consumers know if they want to commit to the loan being offered, and it enables them to make meaningful comparisons between loan products for better shopping. The Bureau received feedback from consumer testing, through the Bureau's website, from a small business review panel, through public comments on the proposed rule, and from other supplemental outreach.

Improved consumer understanding

An extensive study confirmed the benefits of the new CFPB forms. Consumers of all different experience levels, with different loan types – whether focused on buying a home or refinancing – were able to understand CFPB's new forms better than the current forms. Testing showed that participants who used the CFPB's new forms were better able to answer questions about a sample loan – a statistically significant improvement of 29 percent. Importantly, they were better able to decide whether they can afford the loan, including the cost of the loan over time. And, specifically, the forms help consumers better understand key information:

- **Risk factors:** Because information on the CFPB forms is disclosed in an easy-to-read format, consumers can more easily identify risky loan features. In addition, lenders will have to tell homebuyers about prepayment penalties, larger-than usual periodic payments, and complicated loan structures.

- **Short-term and long-term costs:** By putting the important information in a clearer format than the current forms and in plain language, both the Loan Estimate and Closing Disclosure more easily explain the total costs of the loan. This includes an important breakdown of the loan amount, the principal and interest payment, and how it could change, and closing costs.

- **Monthly payments:** The CFPB forms state in bold font what a consumer's monthly principal and interest payments will be. If it is an adjustable-rate loan, the forms say the projected minimum and maximum payments over the life of the loan.

Better comparison shopping

When consumers understand their loan offers, they can better compare competing offers. In testing, the CFPB's new forms performed better than the current forms when it comes to comparing competing offers by as much as 42 percent. This leads to better consumer choice. The forms enable better:

- **Comparisons of competing loan offers:** The new forms use formatting that clearly breaks down the costs of the loan, such as the interest rate, mortgage insurance costs, and closing costs. As a result, would-be-homebuyers and those refinancing their existing mortgage are better able to distinguish between two different loan offers.

- **Shopping for closing costs:** Closing costs are the costs of completing a mortgage transaction, including origination fees, appraisal fees, title insurance, taxes, settlement services, inspections, and homeowner's insurance. Consumers can save money if they shop around for their own service providers for some of these costs. The CFPB forms plainly outline what closing services a consumer will need and which ones they can shop around for.

Avoiding costly surprises at the closing table

With the current forms, consumers can have a hard time comparing their original loan terms to their final loan offer. Consumers need to be reasonably sure that the mortgage they signed up for is the one they are getting. The CFPB's rules curtail "bait and switch" tactics, where the terms change at closing, by implementing several new consumer protections:

- **Easier comparisons of the estimated and final terms of the loan:** By making the Loan Estimate and Closing Disclosure very similar in format, consumers are better able to compare their estimate with the final terms of the loan. In testing, the CFPB's new forms performed better than the current forms when it comes to comparing estimated and final numbers by as much as 28 percent.

- **More time to consider choices:** By providing the Closing Disclosure three days before closing, consumers can review their final loan terms and costs in an unpressured environment rather than at the closing table. This allows consumers time to confirm whether they are getting what they expected. It also gives consumers time to ask questions and negotiate over changes that have occurred. This is especially true for consumers who are refinancing and can more easily delay the closing of the loan.

- **Limits on closing cost increases:** Today's rule restricts circumstances in which consumers can be required to pay more for settlement services than the amount stated on their Loan Estimate. Lenders cannot impose new or higher fees on the final loan unless there is a legitimate reason.

Today's rule is effective Aug. 1, 2015 and the CFPB is already working with industry and consumers toward effective implementation. As the CFPB continues with "Know Before You Owe," it will work collaboratively with all, including other government stakeholders, to take a close look at all documents provided at closing.

Today's rule is a continuation of the CFPB's efforts to reform the mortgage markets. In January 2013, the CFPB released new rules on mortgage servicing, mortgage loan origination compensation, and the mortgage origination process. Today's rule and new forms are just one part of the CFPB's efforts to make the mortgage market work better for consumers, the industry, and the economy as a whole.

A factsheet about the "Know Before You Owe" mortgage disclosures is available at:
http://files.consumerfinance.gov/f/201311_cfpb_factsheet_kbyo_mortgage-disclosures.pdf

A factsheet about the testing process the CFPB used to arrive at today's rule is available at:
http://files.consumerfinance.gov/f/201311_cfpb_factsheet_kbyo_testing.pdf

The "Know Before You Owe" mortgage disclosure rule will be live on Wednesday at:
http://files.consumerfinance.gov/f/201311_cfpb_final-rule_integrated-mortgage-disclosures.pdf

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The Consumer Financial Protection Bureau is a 21st century agency that helps consumer finance markets work by making rules more effective, by consistently and fairly enforcing those rules, and by empowering consumers to take more control over their economic lives. For more information, visit consumerfinance.gov.