executive **summary**

Consumer Testing of the **Good Faith Estimate** and **HUD-1** Forms

in this report…

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executive **summary**

In 2002, the Department of Housing and Urban Development (HUD) published its proposed rule under the Real Estate Settlement Procedures Act (RESPA) to simplify and improve the process of obtaining home mortgages and to reduce settlement charges for consumers. Because a policy aimed at benefitting consumers through improved disclosures is only as good as the documents consumers see, HUD's Offices of Housing, General Counsel, and Policy Development and Research began working on a standardized research-based, consumer-tested Good Faith Estimate (GFE) to replace the wide variations of GFEs in current use. With HUD estimating approximately 12.5 million settlements covered by RESPA in a typical year, the Agency wanted to provide consumers with information in a readily understandable language and format.[1] Its goal was that consumers could do the following:

- Compare the offers they receive through a standard GFE document
- Identify key loan details, such as variable rates, balloon payments, and prepayment penalties
- Identify loans with the lowest settlement charges
- Understand the variables that could affect settlement charges
- Identify the tolerances on changes from the GFE estimated settlement charges to the HUD-1 final settlement charges
- Identify the charge or credit from both lenders and brokers that are linked to a particular interest rate
- Understand the benefits of shopping for multiple loan offers

In a commitment to continuous improvement, HUD undertook a three-phased study to iteratively test the new GFE over six years from August 2002 until September 2008.[2] This testing included qualitative interviews and small testing groups with nearly 1,600 homebuyers, potential homebuyers, and homeowners who had refinanced in 17 cities across the United States. It included large, urban locations, such as Atlanta, Georgia, Boston, Massachusetts, Chicago, Illinois, and Seattle, Washington, as well as smaller urban areas, such as Birmingham, Alabama, Tulsa, Oklahoma, and Wilmington,

[1] See http://www.realtor.org/research/research/ehsdata

[2] HUD initially contracted with Aspen Systems on an existing contract, and Aspen Systems subcontracted with Kleimann Communication Group, Inc. (KCG) for Phases 1 and 2. For Phase 3, HUD contracted directly with KCG.

Delaware. In all rounds of testing, the demographics of participants represented a cross-section of the American homebuying population in terms of age, race, income, and education.

Throughout the three phases of the study, HUD and the Aspen/KCG team shared their contributory expertise to ensure that the consumer-driven GFE was rooted in technical accuracy. The GFE translated complex concepts and content into words that consumers understood and preferred; it used a visual presentation coupled with those words to reinforce and emphasize the key information. The intent was always that consumers would use supplemental materials to deeply understand the details of their loan and settlement charges, but the GFE was to be sufficiently independent and clear that consumers would know to ask questions and would be able to frame these questions for further clarification.

The final GFE achieves the intended goals. Testing results show that consumers can:

- identify the lowest settlement charges in nearly all instances when shown two GFEs,
- compare across multiple GFEs easily,
- identify key loan details, and
- understand the reciprocal relationship between settlement charges and interest rates.

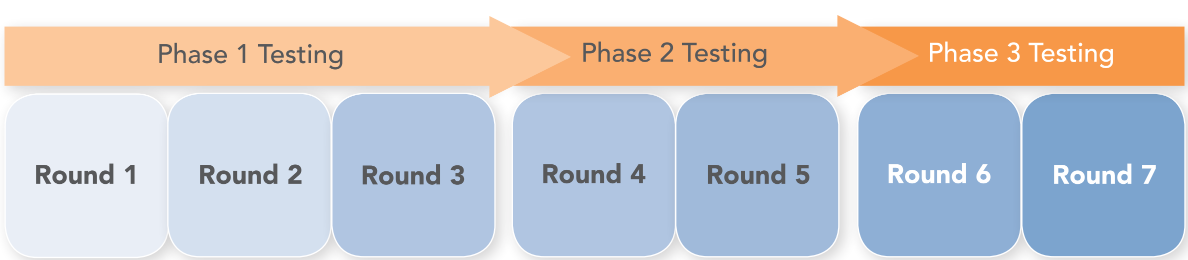
Even more importantly, consumers gain the confidence to ask questions.

Although the revised GFE was clearly intended to assist consumers, it could not introduce an unintended bias against either brokers or lenders as a result of the yield spread premium (YSP)/ discount points disclosure. These disclosures are critical to consumers' understanding of the relationship of the interest rate of the loan and the amount of the total estimated settlement charges. Importantly, with the final GFE, consumers will choose a loan that reveals the YSP as readily as they will chose a loan that does not reveal the YSP.

Discussion of Results

In August 2002, HUD began work with the Aspen/KCG team to develop and iteratively test a consumer-focused and validated GFE. In a process of continuous improvement, the GFE's design and content evolved over the three phases paralleling policy refinements to the rule within HUD and the results of the consumer testing:

- Phase 1: Formative testing and development
- Phase 2: Quantitative validation
- Phase 3: Responses to the environment



Phase 1: Formative Testing and Development Rounds 1, 2, and 3 of Testing August 2002–March 2003

In this phase, Aspen/KCG identified, through consumer testing, language choices and initial visual presentations of information that increased participants' comprehension and ability to select loans with lower settlement charges with all other variables held constant. Over three rounds of testing, Aspen/KCG tested 150 participants in 10 cities,[3] using comprehensive one-on-one interviews with participants. During this phase, we also tested a form for a Guaranteed Mortgage Package Agreement (GMPA), later revised and renamed Mortgage Package Offer (MPO)—which HUD subsequently withdrew from consideration. At the end of this phase, the basics of the GFE were in place: the design, loan details, settlement charges, a tolerance table, and a tradeoff table.

Phase 1 at a Glance

What We Did in Rounds 1, 2, and 3 of Testing

Using qualitative research interviews, the Aspen/KCG team experimented with alternate ways of presenting information to homebuyers so that they could do the following:

- identify key loan details,
- identify loans with lowest total settlement charges,
- understand the relationship between interest rates and settlement charges,
- understand the YSP's relationship to origination charges for lenders and brokers, and
- identify limits to changes that can occur between the GFE and the HUD-1.

Working with HUD, Aspen/KCG developed an initial GFE to reflect the evolving RESPA policy. The goals through these first three rounds of testing were to identify the information participants found important, get initial reactions to the design and language of the GFE, and measure performance on key elements, especially consumer understanding of the YSP and discount points. After each round of testing, HUD and Aspen/KCG would use the qualitative results of the research to revise the language and design of the GFE and to set goals for the next round of testing.

What We Found in Rounds 1, 2, and 3 of Testing

Across the three rounds of testing, participants enthusiastically liked the GFE and felt that it was an improvement on GFEs that they had seen previously. They called the language appropriate and understandable, making them feel comfortable that they could use it. They also commented

[3] Round 1 cities: Baltimore, MD; Birmingham, AL; Chicago, IL. Round 2 cities: Austin, TX; Portland, OR; San Diego, CA. Round 3 cities: Los Angeles, CA; Minneapolis, MN; Tulsa, OK; Wilmington, DE.

positively on the design of the GFE and MPO, saying that they were clear and easy to use, specifically the tables that summarized loan details and provided a breakdown of the settlement charges. Participants identified the tradeoff table as one of the most helpful elements, using it to understand that alternative loans could exist and that they could adjust the amount of their settlement charges by choosing different interest rates. Some participants saw the advantage of reducing their settlement charges by taking a higher interest rate, while others preferred reducing their interest rate and paying higher settlement charges. Nearly all participants responded positively to the idea of the tolerances which set limits on the charges that could change at the actual settlement.

Although most participants had heard of "points," their understanding of this fairly complex concept was marginal. Additionally, most participants did not understand the alternate explanations of YSP and discount points provided throughout the three rounds of testing. In none of the three rounds of testing did more than 50.0% of the participants show clear understanding of the explanations. Table 1 below shows how participants performed in key areas when using the GFE throughout Phase 1.

Table 1. Participant Performance on Key Elements in Phase 1

	Identify total settlement charges	Understand the tradeoff table	Understand tolerances	Understand YSP and discount points
Round 1 (n = 45)	91.0%	62.0%	48.0%	40.0%
Round 2 (n= 45)	97.0%	67.0%	70.0%	50.0%
Round 3 (n = 60)	N/A	86.0%	66.0%	40.0%

The Resulting GFE (March 2003)

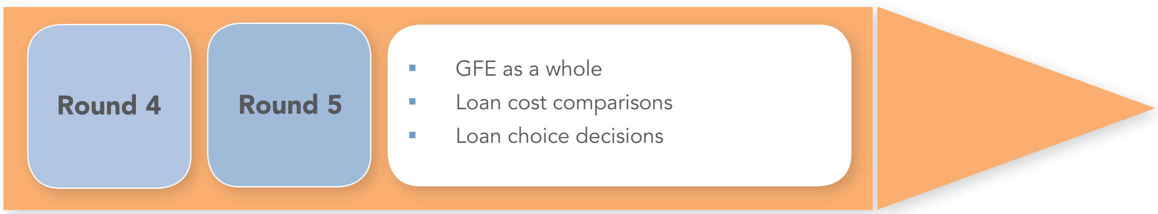
Because of continued poor performance in the sections explaining discount points and YSP, these sections were removed from the GFE. As a result of Rounds 1, 2, and 3 testing over 8 months, the GFE consisted of the following components:

- Page 1 provided a one-page summary of key information about the loan. It included identification information, basic information about the GFE and its purpose, a summary of loan details, and a three-line summary of total estimated settlement charges that showed the originator's service charge, all other settlement charges, and the total estimated settlement charges.
- Page 2 of the GFE provided details about settlement charges including two options in Item 2 for disclosing the charge or credit for the interest rate. Eight categories of all other settlement charges were also listed with brief explanations of each category.
- Page 3 provided details about the tolerances (how much charges could change between the GFE and settlement), a tradeoff table that showed the relationship of interest rate to settlement charges, and information on how to proceed with the loan application.

Phase 2: Quantitative Validation
Rounds 4 and 5 of Testing
October 2003–March 2004

During 2003, the Federal Trade Commission (FTC) completed a study of consumer response to the disclosure of the YSP on the GFE.[4] This FTC study used only an extract of HUD's Phase 1 GFE. In response, HUD initiated two quantitative studies in Phase 2 to parallel FTC's study but used a complete and revised version of the GFE. During Round 4 and Round 5, Aspen/KCG tested 1,200 participants in five cities,[5] using quantitative testing groups.

Rounds 4 and 5 at a Glance



What We Did in Round 4 of Testing

In Round 4 of testing, HUD asked Aspen/KCG to parallel aspects of the FTC study, including the questions asked, the difference between amounts of each offer, and the length of the test situation. In the HUD study, participants were given an entire GFE, not just an extract as the FTC study had done. Using the entire form allowed HUD's study to better discern whether participants could distinguish the salient information in the disclosure and also show whether the contextual information in HUD's GFE was necessary.

Participants were divided randomly into a control group and an experimental group. In the control group, 285 participants were given two sets of GFEs that did *not* contain the YSP disclosure, one in which the broker loan was $300 less and one set in which each loan cost the same. In the experimental group, 315 participants were given two sets of GFEs that contained the YSP disclosure, one in which the broker loan was $300 less and one set in which each loan cost the same. The same cost loan was included as a more rigorous test of potential bias between a broker-originated and a lender-originated loan; in reality borrowers are highly unlikely to receive two loan offers in which all aspects of the loan offers are identical. Aspen led all groups and asked each group's participants to write down their answers to three questions: (1) which offer was cheaper, or do they cost the same?; (2) Which would you choose ?; and (3) Why did you make that choice?

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[4] James M. Lacko and Janis K. Pappalardo, The Effect of Mortgage Broker Compensation Disclosures on Consumers and Competition: A Controlled Experiment (Washington, DC: Federal Trade Commission, 2004), http://www.ftc.gov/os/2004/01/030123mortgagefullrpt.pdf (accessed October 10, 2008).

[5] Round 4 and Round 5 cities: Atlanta, GA; Boston, MA; Denver, CO; Seattle, WA; Tulsa, OK.

What We Found in Round 4 of Testing

Results from the testing showed that the HUD-designed GFE performed approximately the same or slightly better than the FTC test results when the YSP was not disclosed, with 91.6% of HUD participants identifying the cheaper loan and 88.1% choosing that same loan. However, the GFE that included the YSP disclosure did much better than the FTC results whether the loans were of different costs (83.2% vs. 71.8%) or the same costs (80.6% vs. 53.4%).

Nonetheless, the results showed that when participants saw the YSP disclosure in a same cost loan, only slightly more than half would choose either loan and nearly 39.3% would default to the lender rather than the broker. An analysis of the qualitative results to question 3 ("Why did you make that choice?") suggested that participants thought that lenders did not have similar kinds of credits or charges. Table 2 below shows the comparison of FTC and HUD test results. The numbers do not add up to 100 because the "other" category is not reported, including participants coded as "non-responsive."

Table 2: Comparison of FTC Results and HUD Round 4 Results

	Without YSP (Percent)		With YSP (Percent)	
Different Cost Loan Comparison (broker lower)	**FTC**	**HUD**	**FTC**	**HUD**
Which loan is cheaper?				
Broker (correct)	90.3	91.6	71.8	83.2
Lender (incorrect)	3.9	0.7	16.5	7.9
Same (incorrect)	5.8	5.6	9.7	6.3
Which would you choose?				
Broker (correct)	85.2	88.1	69.9	72.1
Lender (incorrect)	2.9	0.4	15.5	11.1
Either (incorrect)	3.9	6.3	4.9	11.4

	Without YSP (Percent)		With YSP (Percent)	
Same Cost Loan Comparison (broker/lender same)	**FTC**	**HUD**	**FTC**	**HUD**
Which loan is cheaper?				
Same (correct)	95.1	95.1	53.4	80.6
Broker (incorrect)	1.9	0.7	10.7	2.9
Lender (incorrect)	2.9	1.4	30.1	14.6
Which would you choose?				
Either (correct)	77.7	89.5	25.2	50.4
Broker (incorrect)	6.8	2.1	16.5	5.4
Lender (incorrect)	6.8	1.4	45.6	39.3

The Resulting GFE from Round 4 of Testing (December 2003)

As a result of the Round 4 testing analysis, the GFE retained the same components as at the end of Round 3, but was revised to include an additional checkbox in Item 2 that lenders who did not disclose specified YSP or discount points would be required to check: "The credit or charge for the interest rate you have chosen is included in 'Our service charge.' (See Item 1 above.)"

What We Did in Round 5 of Testing

To validate the change of having three options in Item 2, HUD authorized an additional study of 600 participants in the same five cities. Round 5 repeated the quantitative test of Round 4 and also divided the sample into a control group and an experimental group. The control group received GFEs with two options in Item 2, and the experimental group received GFEs with three options in Item 2. Within each group, participants received multiple sets of two GFES: one in which the lender was lower, one in which the broker was lower, and one in which the loans cost the same.

In addition, we tested whether providing participants with a Mortgage Shopping Chart would improve their performance in identifying the lowest cost loan when more than two loan offers were provided. To test this concept, only the experimental group (three options in item 2 of the GFE) was included. We gave 300 participants in the experimental group one of two sets of four GFEs. For the first set, 150 participants were given four loan offers of which one was a broker loan which cost less. For the other set, 150 participants were given four loan offers of which a broker and a lender loan offer cost the same and were the lowest cost of the four loans. Within each of the groups of 150 participants, 75 were instructed to use the shopping chart and 75 were given a shopping chart but received no explicit instruction to use it.

What We Found in Round 5 of Testing

When three options were in Item 2, participants in the experimental group performed slightly better than participants in the control group who had two options in Item 2. Results showed that participants using the GFE with three options in Item 2 identified the lowest cost loan at least 90.0% of the time, whether the lender or broker had the lower cost or whether the loans cost the same. When asked which loan they would prefer when the two loans had different costs, about 88.0% of these same participants choose the broker correctly when it was lower and chose the lender correctly when it was lower.

In the same cost loan comparison, the results were not as good. With both loans costing the same, participants would be expected to say that they prefer either loan. However, with the control group (two options in Item 2), only 61.4% of them said they would choose either loan offer. With the experimental group (three options in Item 2), 70.2% said that they would choose either loan. Neither result is as good as the results for loans with different costs. The reality is that receiving two identical loans is highly unlikely. In the more realistic scenario of receiving two loan offers which are different, 87.3% of the participants chose the broker loan when it was lower, and 88.6% of participants chose the lender loan when it was lower. Table 3 below shows the detailed results, but the numbers do not add up to 100 because the "other" category is not reported, including participants coded as "non-responsive."

Table 3. Differences Between the Two-Option YSP and the Three-Option YSP, Two-Loan Comparisons in Round 5

Different Cost Loan Comparison (broker lower)	Two-option YSP (Percent)	Three-option YSP (Percent)
Which loan is cheaper?		
Broker (correct)	90.7	91.6
Lender (incorrect)	3.5	4.3
Same (incorrect)	4.5	2.7
Which would you choose?		
Broker (correct)	86.3	87.3
Lender (incorrect)	2.8	6.7
Either (incorrect)	4.5	3.7
Different Cost Loan Comparison (lender lower)	**Two-option YSP (Percent)**	**Three-option YSP (Percent)**
Which loan is cheaper?		
Lender (correct)	88.9	92.3
Broker (incorrect)	2.1	1.0
Same (incorrect)	7.6	6.0
Which would you choose?		
Lender (correct)	86.1	88.6
Broker (incorrect)	2.1	0.3
Either (incorrect)	6.3	8.1
Same Cost Loan Comparison (broker/lender same)	**Two-option YSP (Percent)**	**Three-option YSP (Percent)**
Which loan is cheaper?		
Same (correct)	85.3	90.0
Broker (incorrect)	3.4	1.0
Lender (incorrect)	8.5	7.0
Which would you choose?		
Either	61.4	70.2
Broker	6.8	3.6
Lender	23.9	21.2

In the second part of the study, results for the four-way comparison with and without the use of the Mortgage Shopping Chart showed some variance in performance. When the broker loan was the lowest of four offers, without the shopping chart 91.9% of the participants correctly identified it as the lowest cost. When instructed to use the chart, 97.4% identified correctly the lowest cost loan. Table 4 below shows the detailed results of the four-loan comparison with the broker lower, but the numbers do not add up to 100 because the "other" category is not reported, including participants coded as "non-responsive."

Table 4. Difference When Participants Did or Did Not Receive Instructions to Use the Mortgage Shopping Chart, Four-Loan Comparison with Broker Lower in Round 5

Four-form Different Cost Loan Comparison (broker lower)	Number	Percent
Which offer costs less? *Participants not instructed to use Mortgage Shopping Chart*		
B$6,100 (correct)	68	91.9
L$6,400 (incorrect)	2	2.7
L$6,500 (incorrect)	1	1.4
B$6,900 (incorrect)	0	0.0
Four-form Different Cost Loan Comparison (broker lower)	**Number**	**Percent**
Which offer costs less? *Participants instructed to use Mortgage Shopping Chart*		
B$6,100 (correct)	75	97.4
L$6,400 (incorrect)	0	0.0
L$6,500 (incorrect)	0	0.0
B$6,900 (incorrect)	0	0.0

In the same experiment, when two of the four loans were the same cost, 89.5% correctly identified the lender or the broker as the lowest cost loans. When participants were told to use the shopping chart, correct identification rose to 92.2%. Table 5 below shows the detailed results of the four-loan comparison with two loans costing the same, but the numbers do not add up to 100 because the "other" category is not reported, including participants coded as "non-responsive."

Table 5. Difference When Participants Did or Did Not Receive Instructions to Use the Mortgage Shopping Chart, Four-Loan Comparison with Two Same Cost Loans in Round 5

Four-form Same Cost Loan Comparison (broker/lender same)	Number	Percent
Which offer costs less? *Participants not instructed to use Mortgage Shopping Chart*		
B$6,500 (correct)	31	40.8
L$6,500 (correct)	37	48.7
B$6,900 (incorrect)	1	1.3
L$6,600 (incorrect)	4	5.3
Four-form Same Cost Loan Comparison (broker/lender same)	**Number**	**Percent**
Which offer costs less? *Participants instructed to use Mortgage Shopping Chart*		
B$6,500 (correct)	44	57.2
L$6,500 (correct)	27	35.0
B$6,900 (incorrect)	2	2.6
L$6,600 (incorrect)	2	2.6

The Resulting GFE (March 2004)

As a result of testing in Rounds 4 and 5 over six months, the GFE consisted of the following components:

- Page 1 provided a one-page summary of key information about the loan. It included identification information, basic information about the GFE and its purpose, a summary of loan details, and a three-line summary of total estimated settlement charges that included the originator's service charge, all other settlement charges (from page 2), and the total estimated settlement charges.
- Page 2 provided details about settlement charges including three options for disclosing the charge or credit for the interest rate in Item 2. Eight categories of all other settlement charges were also listed with brief explanations of each category.
- Page 3 provided details about the tolerances (how much charges could change between the GFE and settlement), a tradeoff table that showed the relationship of the interest rate of the loan to settlement charges, and information on how to proceed with the application.
- Page 4 was added with a Mortgage Shopping Chart to help consumers compare multiple loans.

Phase 3: Responses to the Environment
Rounds 6 and 7 of Testing
October 2007–October 2008

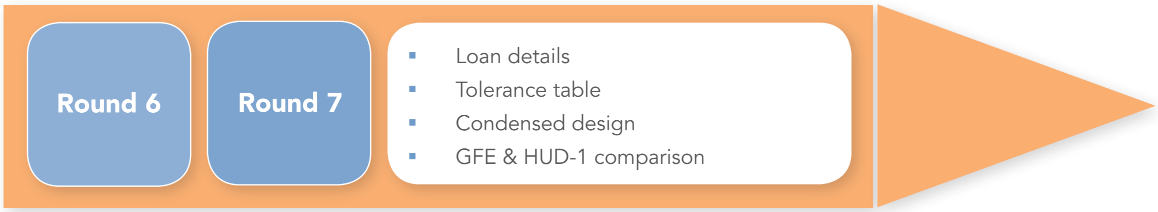
In March 2004, HUD withdrew the proposed RESPA rule pending further consultations with industry, consumer groups, and the public. With a serious consideration of public concerns, but faced with emerging difficulties in the mortgage market, HUD renewed its efforts to revise its RESPA regulations and the GFE. In October 2007, HUD considered adding to the RESPA rule the requirement of a closing script to help consumers match the estimates of the GFE to the actual charges of the HUD-1.

HUD contracted with Kleimann Communication Group, Inc. (KCG) to adapt the GFE to reflect additional changes in response to the market and public comments and to conduct a Round 6 test of the GFE, the HUD-1, and the closing script in November 2007. The primary changes were adding information to the loan details sections, clarifying the settlement charge descriptions on page 2, and continuing to refine the tolerance presentation.

Based on the results of Round 6 testing, HUD published its proposed RESPA reform rule with a revised GFE and closing script in the *Federal Register* in March 2008. Public comments were accepted until June 2008. With these comments, HUD continued to adapt the rule and the GFE through July and August 2008. Most importantly, HUD responded to comments about the length of the GFE by shortening it from four pages to three: maintaining the one-page summary (page 1) and the one page of settlement charges details (page 2), and consolidating the tolerances, the tradeoff table, and the shopping chart onto a single third page. At the end of August, HUD sent the draft final rule and the shortened GFE to the Office of Management and

Budget (OMB) for review. During the review, HUD directed KCG to conduct a Round 7 test of the continuous improvement changes to the GFE and to document the performance of the GFE.

Rounds 6 and 7 at a Glance



What We Did in Round 6 of Testing

In Round 6, Test 1, KCG tested the four-page Revised GFE and a two-page Alternate GFE with 60 participants in three cities.[6] In each site, 10 participants used the Revised GFE and 10 the Alternate GFE. During the one-on-one cognitive interviews, participants were asked to think aloud as they read through a single GFE. They were then asked a series of structured questions about aspects of the GFE to ascertain their understanding. They were then given two additional GFEs and asked to identify which loan of the three was cheaper and which loan they would choose. Half of the sets of three had the broker with lowest cost and half had the lender with lowest cost.

In Round 6, Test 2, 20 participants in two different cities worked with the new script to determine if it helped consumers at settlement to compare the GFE and the HUD-1 in order to identify changes to the loan details or settlement charges which had increased beyond the tolerance limits defined in the GFE.

What We Found in Round 6 of Testing

For Test 1, participants tended to perform better on the four-page Revised GFE than on the two-page Alternate GFE. When shown three Revised GFEs, 100% correctly identified and 100% correctly chose the broker loan as cheaper. On the Alternate GFE, 86.0% of the participants correctly identified and 80.0% chose the broker loan. When the loan comparison had the lender lower, the two forms performed similarly. However, the Alternate GFE caused various problems around the discount points and the YSP. Moreover, participants with the Alternate GFE had somewhat greater difficulty understanding the tolerances.

For the Revised GFE, participants enthusiastically supported the standardization of the design of the GFE for reducing the difficulty of comparisons. They also commented positively about the length, the layout, the language, and the tradeoff table. Participants liked the Mortgage Shopping Chart, but thought that six loan options for comparison were too many. Participants also were unsure of the meaning of some dates, even though 70.0% of them could identify how long the interest rate was available.

[6] Round 6, Test 1 cities: Atlanta, GA; Boston, MA; Denver, CO. Round 6, Test 2 cities: Cincinnati, OH; Phoenix, AZ.

For Test 2, participants liked having the script read to them, but struggled with managing the GFE, the HUD-1, and the script when asked to use paper formats. However, participants liked the crosswalk table format of the paper version of the closing script and saw it as beneficial.

The Resulting GFE from Round 6/Proposed Rule (March 2008)

Based on these results, HUD and KCG made several changes to the GFE. This version of the GFE was published in the *Federal Register* in March 2008 as part of the proposed RESPA rule.

- Page 1 remained a summary of key elements about the loan and GFE. All important dates were grouped together to emphasize the time deadlines and provide a checklist of important dates for consumers. The summary of loan terms added details about monthly escrow and the possibility of interest rate and loan balance rising. A three-line summary of total estimated settlement charges showed the service charge, all other settlement charges, and the total estimated settlement charges.
- Page 2 provided details about settlement charges including three options for disclosing the charge or credit for the interest rate in Item 2. Refinements to the categories of all other settlement charges resulted in eight categories listed with brief explanations of each category.
- Page 3 provided details about the tolerances or how much charges could change between the GFE and settlement, a tradeoff table that showed the relationship of interest rate to settlement charges, and information on how to proceed with the loan application.
- Page 4 added information about the other financial responsibilities of homeownership and what happens if the loan is sold in the future. The Mortgage Shopping Chart remained to help consumers compare multiple loans.
- HUD developed a closing script to help guide consumers through the loan details and the actual settlement charges to be used at the time of settlement.

The Resulting GFE and Closing Script after Public Comments, Submitted to OMB (August 2008)

After public comments were received and analyzed, changes were made to the proposed GFE to take the comments into account. Most importantly, in order to respond to expressed concerns about the length of the GFE, the tested structure of the GFE was reduced to three pages with some significant changes:

- Page 1 remained a summary of key loan details (including escrow), but the Summary line for estimated settlement charges was reduced to one line while the "other financial responsibilities" disclosure from page 4 of the proposed rule GFE was incorporated into an expanded escrow account disclosure on page 1.

- Page 2 provided details of the settlement charges. It retained the three options in Item 2 and increased the categories of all other settlement charges to nine by separating "Government recording and transfer charges" into two separate items.

- Page 3 was condensed to include a very abbreviated tolerance chart, the tradeoff table, the shopping chart, and the post-settlement sale of loan disclosure.

- Page 4 of the proposed GFE was deleted.

The closing script was withdrawn, but a new page 3 to the HUD-1 was designed that would help consumers compare loan details and settlement charges between the GFE and the HUD-1. Page 3 of the HUD-1 included a table devised to identify the percentages of change between estimated and actual charges and to identify if the total was within the tolerance limits.

What We Did in Round 7 of Testing (August–September 2008)

To validate these substantive changes to the GFE, HUD authorized a Round 7 test of mixed methodology: qualitative interviews similar to Rounds 1, 2, 3, and 6 and testing groups to quantify performances similar to the quantitative testing in Rounds 4 and 5. The quantitative testing would also test the performance of page 3 of the HUD-1.

In August 2008, KCG performed a pretest of the form sent to OMB for review with the draft final rule. It consisted of seven qualitative interviews and 30 participants in a structured testing group in Denver, Colorado. A GFE form based on this pretest was the subject of the remaining tests. In September 2008, Round 7 testing combined 21 qualitative interviews to diagnose participant issues and a quantitative sample of 90 participants who were given a test in two parts: Part A to test performance on identification and choice in order to look for choice bias; Part B to validate page 3 of the HUD-1. Round 7 also tested a change to the policy of the rule that would allow loan originators the option of filling out the tradeoff table of similar loans with different interest rates and settlement charges. As a consequence, in the qualitative testing, we specifically showed participants GFEs with tradeoff tables that were filled out and tradeoff tables that were left blank to identify if participants noticed the differences and adjusted their choice of loan. Because of earlier criticism that testing varied only settlement cost, we included one set of GFEs in which one GFE was an adjustable rate loan offer in the qualitative testing.

Participants in the quantitative study looked at GFEs in which the lender loan does not show the YSP and the broker loan discloses the YSP. In Part A, participants looked at four sets of GFEs: (1) two GFEs with lender settlement charges lower than the broker; (2) two GFEs with the broker loan lower; (3) two GFEs with the same settlement charges but different loan interest rates; and (4) a four-loan test with one lender and one broker tied with the lowest settlement charges. Participants were asked the now standard questions of (1) Which loan costs less? (2) Why? (3) Which loan would you prefer? (4) Why?

In addition, participants in the quantitative testing were given a second test. It consisted of a GFE and a revised HUD-1 which incorporated the new page 3 in the draft final rule instead of the closing script from the proposed rule. We split the sample into four groups to test two variations of loan details and differences in the settlement charges between the GFE and HUD-1. The HUD-1 mirrored the details of the GFE exactly except for one these four details:

- The prepayment penalty increased from $2,000 to $4,000
- The interest rate and monthly payment increased from 6.5% ($632.07 per month) to 6.75% ($648.60 per month)
- Charges for items 3 through 7 increased by 11%
- Charges for items 3 through 7 increased by 8%

Participants were asked to identify (1) if there was a change between the two documents, (2) what the change was, (3) if that change was allowed, and (4) if they would move forward with the HUD-1 at settlement and why.

What We Found in Round 7 of Testing

Qualitative Results. In Round 7, across the four sites, participants overall understood the information in the GFE, compared information across GFEs, and identified and chose a loan offer based on lowest cost whether a broker-originated or lender-originated loan. Participants were easily able to identify the adjustable rate loan offer, and no one selected it. Participants far preferred to have the tradeoff table filled out than to have it blank. Participants tended to choose the loan offer that had a completed tradeoff table, expressing some suspicion when it was not completed.

In the Denver pretest, two elements did not perform well: the escrow information on page 1 and the tolerance table on page 3. For the escrow information, participants needed more details and were unclear how the information on page 1 related to the escrow item on page 2. Since this language had been added to the GFE in response to public comment and had not been previously tested, we anticipated needing to modify the language for the remaining tests. More importantly, the tolerance table, which had worked well in Round 5 of testing, simply did not work in the abbreviated version introduced to reduce the length of the GFE from 4 pages to 3. Participants had difficulty looking at the item number in the chart on page 3 and matching it to the description on page 2.

For the remaining three test sites, we modified the escrow language and drastically reworked the design of the tolerance table. We embedded zero-tolerance information in the description of the items on page 2, added graphic elements on page 2 to “flag” other tolerances, and shifted the tolerance language on page 3 to focus on the items with a 10% tolerance.

However, in the final three test sites, neither set of changes was successful. For the escrow disclosure, participants continued to be confused. For the tolerance table, participants did not complain about the switching between pages, but primarily because they skipped over the text about tolerances on the top of page 3. Most did not notice the graphic elements on page 2; when they did, they disliked them; and they were not able to accurately identify zero-tolerance and no-tolerance items.

Quantitative Results, Part A, Two-Loan Comparison. In the quantitative testing, Denver participants uniformly did better than in the other three sites. Of Denver participants who received a loan offer in which the broker loan was lower, 86.7% identified it as costing less and 96.7% chose the lower cost loan. When the lender loan was lower, 90% identified it correctly and 90% chose the lower loan. These performance levels were quite close to the percentages in Round 5 of testing as seen in the first two columns of Table 6 below.

Although the Denver pre-test sample is too small to detect statistical differences from the rest of Round 7, the performance in the other three sites is quite different. In these sites, 82.2% of participants given two loan offers in which the broker was less **identified** correctly the lower cost loan; when the lender was lower, the same percentage (82.2%) of participants identified correctly the lower cost loan. Participants also **chose** the lower loan offer at nearly equal rates: 82.2% for the broker lower and 80.0% for the lender lower.

These results are consistent; if participants identified the lower cost loan, they chose the lower cost loan whether from a lender or broker—and at rates that suggest a solidly successful form. However, when we compare the percentages of correct answers with the results from Round 5, the percentages are uniformly lower and demonstrate a statistically significant decline in consumer performance between the two rounds of testing. Table 6 below shows the comparison of Round 5, the Denver pretest, and the remaining three sites.

Table 6. Results of Identification and Choice Questions for Part A, Two-Loan Comparison in Rounds 5 and 7

Different Cost Loan Comparison (broker lower)	Round 5: 3-option YSP (Percent)	Round 7: Denver (Percent)	Round 7: 3 sites (Percent)
Which loan costs less?			
Broker (correct)	91.6	86.7	82.2
Lender (incorrect)	2.7	10.0	4.4
Same (incorrect)	4.3	3.3	8.9
Which loan would you prefer?			
Broker (correct)	87.3	96.7	82.2
Lender (incorrect)	3.7	3.3	3.3
Either (incorrect)	6.7	—	11.1

Different Cost Loan Comparison (lender lower)	Round 5: 3-option YSP (Percent)	Round 7: Denver (Percent)	Round 7: 3 sites (Percent)
Which loan costs less?			
Lender (correct)	92.3	90.0	82.2
Broker (incorrect)	1.0	6.7	4.4
Same (incorrect)	6.0	3.3	8.9
Which loan would you prefer?			
Lender (correct)	88.6	90.0	80.0
Broker (incorrect)	0.3	10.0	1.1
Either (incorrect)	8.1	—	14.4

To explore the differences in performance, a further qualitative analysis of participant responses to the question of "Why did you make that choice?" suggested two important factors. One factor was the removal on page 1 of the summing lines for the settlement charges. Participants frequently searched the form looking for total cost information and missed that "Total Estimated Settlement Charges" at the bottom of page 1 referred to the sum of all items on page 2. Without this reminder, the comments showed that participants often went to the "Origination Charge" in Item 1, page 2 to answer the question of "Which loan costs less?" When the three lines were included on page 1, as was true in Round 5, participants tended to perform better.

The other factor emerging from the comments was the influence of the zero-tolerance language into Items 1 and 2, page 2. This language led some participants to believe that their adjusted origination charge could not change with a lender loan and could change with a broker loan, thus influencing some responses to "Which loan would you prefer?"

But neither of these factors sufficiently and logically explains the consistently lower performance in the three sites. The next question to ask is was there a major difference between what was on the form when we tested in the three sites as opposed to Denver or in Round 5? Only one major element varies—the presentation and location of the tolerance information. When integrated into page 2, performance falls consistently across the loans. When located on page 3, performance is at the levels of Round 5 which also located the tolerance information on page 3. (See *Consumer Testing Results for HUD's Good Faith Estimate (GFE) Form: Rounds 6 and 7* for a more thorough discussion of why this change affected performance.)

Quantitative Results, Part A, Four-Loan Comparison. In the four-loan comparison, we saw similar evidence of differences in performance. Of the 90 participants, nearly half (46.7%) recognized that two out of four loans had the same lowest settlement charges and identified them both. 32.2% identified only the correct lender loan as having lower settlement charges, and 17.8% identified only the correct broker loan as having lower settlement charges. In total, 96.7% correctly identified loans with lower settlement charges. When choosing a loan, the proportion remains about the same. Of the 80 participants who chose,[7] 36.3% said that they would chose either of the lower cost loans; 45.0% said they would choose the lender loan; 13.8% said they would chose the broker loan; and only 5.0% had a completely wrong answer. Although these results suggest that 95.0% of the participants would choose a lower cost loan, the distribution of choice was puzzling.

A further analysis of the participant responses to the question of "Why did you make that choice?" suggested three possible factors similar to those in the two-loan comparisons. The first factor tied back to the removal on page 1 of the summing lines for the settlement charges. Without a reminder that cost was determined by the sum of all settlement charges, some participants went to the "Origination Charge" in Item 1, page 2 to assess lowest cost and made their choice based on that cost. The second factor is similar to the two-loan comparisons: in the test version, language about tolerances was inserted into Box 2 and led some participants to believe that their adjusted origination charge could not change with a lender loan, but

[7] The lower number of participants (80 instead of 90) for only the four-form comparison resulted from differences in how the identical cost loans were presented to participants in the first testing group in Atlanta. This presentation was changed for subsequent testing groups in Atlanta.

could with a broker loan. However, the analysis also showed a third factor emerging from the comments. Based on the information in Item 2, page 2, some participants thought that lenders did not have similar charges or credits for a selected interest rate because Box 1 in Item 2 was not parallel to the other two boxes. No space for the interest rate was included in this line. These three factors—all focused on the same section of the GFE—seem to be interacting influences on choice in this test. These factors for both the two-loan and four-loan comparisons are fundamentally design issues and addressable.

Quantitative Results, Part B. The comparison between the GFE and the HUD-1 clearly showed that participants were concerned if they noticed a change in any of the loan details or settlement charges. Of the 90 participants, 90.0% noticed a change between the GFE and HUD-1, indicating that most participants could move easily from one document to the other.

Of the 90 participants, a total of 70 participants received a HUD-1 with a change from the GFE that increased interest rate, increased the prepayment penalty, or had settlement charges above the tolerance level of 10%. Although 63 noticed the change, 34 correctly identified that the change was a loan term change or outside the tolerance, and only 28 said they would still move forward with the settlement.

The difference between raising the charges $150 (up 8%) or $205 (up 11%) of items 3 through 7 at settlement may have impacted the decision making of the groups with regard to the HUD-1. Of the participants, 65.0% in the group with the 11% increase said they would not move forward with the settlement. In the group with the 8% increase, 55.0% of participants said they would not move forward. In both groups, several mentioned being upset to find that charges had increased between the two documents.

The Final GFE (October 2008)

Based on these results, HUD made final recommended changes to the GFE and the HUD-1 to be published. The GFE would consist of these components:

- Page 1 remains a summary of key loan details. The escrow language now clearly identifies whether the borrower has an escrow account, defines the term “escrow,” and states what to do if the borrower does or does not have an escrow account. The one-line summary for estimated settlement charges is restored to the three-line summary of total estimated settlement charges that includes the adjusted origination charge, all other settlement charges, and the total estimated settlement charges.
- Page 2 continues to provide details of the settlement charges. The three options in Item 2 are retained, but there is now a blank for the specific interest rate to be included in the first option of Item 2. Inserting the blank creates a first option that is parallel to options 2 and 3 in presentation of information. Item 5 is simplified based on a HUD determination, but the remaining items for “All Other Settlement charges” do not change. All tolerance information is removed from this page.

- Page 3 relocates information about "Getting more information." "Getting more information" is moved to page 1 and included as part of "Purpose." The abbreviated tolerance chart has been replaced with the more comprehensive and complete format that worked well in all previous rounds. The tradeoff table, the shopping chart, and "If your loan is sold in the future" are retained.

Page 3 of the HUD-1 is retained as a result of participant performance. However, because participants had difficulty knowing what to do once they had identified a discrepancy, we recommend adding a note to page 3 that says the following:

- ***Note:*** *If you have any questions about the Settlement Charges and Loan Terms listed on this form, please contact your lender.*

Conclusion

The extensive consumer testing across seven rounds with both qualitative and quantitative methodologies and analytic techniques has resulted in a consumer-focused Good Faith Estimate (GFE) that consumers can understand and use. This research documents that the policy changes to RESPA and the accompanying changes to the GFE will not bias consumers in their choice of loan offers. The changes to the HUD-1 further ensure that consumers will be better protected against accidental and unwarranted changes between the estimates of the GFE and the HUD-1 actual charges. In short, the key elements of the final GFE and the HUD-1 are useful for consumers and the mortgage lending industry who serve them:

- The standardization of the design and language of the GFE facilitates loan comparisons.
- Consumers can identify the lowest cost loan when asked to compare more than one GFE.
- Consumers can select the lowest cost loan when asked to compare more than one GFE.
- The summaries of key elements on page 1 of the GFE work. The "Summary of your loan" allows consumers to identify variations in the loan details. The three-line "Summary of your settlement charges" reinforces identification of lowest cost loan offers based on total charges, not merely loan origination charges.
- The details of "Understanding your estimated settlement charges" on page 2 of the GFE are clear to most consumers. Consumers understand the relationship of charges and credits to the interest rate. The inclusion of a box to identify the interest rate for lenders in the first box of Item 2 further enhances their understanding.
- The "Understanding which charges can change" (tolerance) table on page 3 of the GFE allows consumers to identify those items for which they can shop themselves or opt to take the assurance of no more than a 10% increase on the total. The table also helps to identify those charges that cannot change at all, thus providing a level of confidence in the stability of the estimates.

- The "tradeoff table" on page 3 of the GFE allows consumers to understand that alternative loan offer options are available. Most consumers far preferred to have the table filled out, expressing some suspicion when it was not completed. Importantly, the table enhanced understanding of the reciprocal relationship between interest rates and settlement charges.
- The "shopping chart" on page 3 of the GFE helped consumers to identify the key elements to consider when they compare offers. Further, the shopping chart suggests the importance of shopping for a loan offer that best meets a consumer's needs.
- The addition of page 3 to the HUD-1 allows consumers to compare and identify more easily the changes that may have occurred between the GFE and the actual charges at settlement. The addition of a brief note to remind consumers to ask their lenders if discrepancies occur identifies an action for them to take and would increase communication between consumers and their lenders.