Housing Initiative Clinic Briefs

The Consumer Financial Protection Bureau's Proposal For Technology in Homeowner Mortgage Closings

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This Housing Initiative Clinic Brief (1) describes the problems consumers encounter during homeowner mortgage closings, (2) reviews the proposal put forward by the Consumer Financial Protection Bureau (the "CFPB") to improve homeowner mortgage closings through the introduction of technology, and (3) provides recommendations for the proposal's successful implementation.

1. The Problems Consumers Encounter During Homeowner Mortgage Closings

For most people, buying a home is the biggest financial decision of their lives and closing a home mortgage is the most substantial financial commitment they will make. Unfortunately, the mortgage closing process—arduous for all parties involved—is a source of significant consumer confusion and stress.

The CFPB, whose primary mission involves increasing transparency in financial markets and providing means to empower consumers to make solid financial decisions, has conducted research to better understand the problems consumers face in the mortgage closing process.[1] Collected through reviews of consumer complaints, public requests for information, and interviews with consumers and industry stakeholders (settlement agents, lenders, etc.), the CFPB's research found that the following five problems were the most commonly cited:

[1] Consumer Financial Protection Bureau, Mortgage Closings Today (April 2014), at 2, *available at* http://files.consumerfinance.gov/f/201404_cfpb_report_mortgage-closings-today.pdf.

- **Late Document Delivery.** The single most cited problem with the mortgage closing process was the timing of document delivery.[2] Before reaching the closing table, each closing document passes through multiple parties' hands. Too often, the previous party in the process delivers the documents late, creating a ripple effect with negative consequences. Late document delivery causes each party to rush, which can lead to stress, errors, and more delays. Furthermore, consumers frequently do not even see the documents until closing day. In this situation, consumers have only a one-hour closing meeting to review and sign approximately 100 pages of documents.
- **Errors in Documents.** Consumers frequently cited errors in closing documents as a problem. According to document generation providers,[3] even the most common errors, such as misspelled names, require closing agents to return the entire closing package for correction.[4] These errors, especially when they occur at the closing meeting, cause frustration, delays, and even increases in closing costs.
- **Large Number of Documents.** Consumers noted the sheer number of documents included in the closing package as another issue. The closing packages are usually around 100 pages in length and industry stakeholders cite redundancy as one of the main reasons for the excessive number of documents.[5] Many consumers admitted that they stopped engaging in the process before it finished.
- **Difficult to Understand Documents.** Consumers also stated that the closing package documents were difficult to comprehend. Many found the document's language to be

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[2] Id. at 20.
[3] Document generation providers are the vendors that provide the lenders and settlement agents with the closing packages for individual mortgages. Id. at 21.
[4] Id.

designed for lawyers, instead of the average consumer, so that finding and digesting the most relevant information was a challenge.

- **Lack of Available Educational Resources.** Consumers reported that there were insufficient educational resources available to them during the mortgage closing process. According to many, loan officers and other key participants were difficult to reach, and no one was available to answer clarifying questions or provide explanations regarding the process. In the end, consumers felt like they had no choice but to sign documents that they did not fully understand.

2. The CFPB's Proposal

After identifying the problems that consumers most frequently encounter during the mortgage closing process, the CFPB set to work on finding solutions. In April 2014, the CFPB announced its proposal to shift traditional closings to a more paperless process through the use of eClosings.[6]

In an eClosing, consumers would receive electronic documents through some form of electronic delivery—for example, by email or by logging into an online portal. The in-person closing meeting would still take place; however, document review would occur on an electronic platform that allows electronic signatures and electronic notarization. Lastly, the completed closing documents would be stored electronically.

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[5] Id. at 22.

a. The Advantages of eClosings

eClosings will directly address four of the five problems with the mortgage closing process identified by the CFPB's research.[7]

First, eClosings allow consumers access to closing documents prior to closing. eClosings' electronic delivery eliminates time delays from mailing hard copies and the electronic platform feature gives multiple parties simultaneous access to the documents. Earlier document delivery should allow consumers to have ample time to review documents prior to the closing meeting. Furthermore, more time means that consumers can review the documents in multiple sessions, so that the large package of documents is more digestible.

Second, shifting to an eClosing process will reduce the frequency of errors in closing documents. As the process and documentation of traditional mortgage closings is increasingly automated, errors resulting from manual processes will be nearly eliminated and the detection of discrepancies will become easier. As a result of decreasing errors, closings will require less time and effort and cost savings may be passed on to consumers in the future.

[6] Marc Patterson, CFPB Announces New eClosing Mortgage Initiative (April 24, 2014), *available at* http://www.cfpbmonitor.com/2014/04/24/cfpb-announces-new-eclosing-mortgage-initiative/.

[7] eClosings will not reduce the number of documents included in closing packages. First, the CFPB does not have control over the vast majority of the documents found in closing packages; so, any significant reduction in the number of documents would require the cooperation of the other entities who do control the vast majority of the documents (lenders, state governments, etc.). Second, the removal of some documents from closing packages would require statutory change. Last, the market does not have a "standard" closing package, so streamlining closing packages across the board would require a commitment from a large number of industry participants. CFPB at 29.

Third, the eClosings' electronic platform creates an opportunity to embed educational tools within the documents that emphasize key information, walk consumers through difficult concepts, and link to additional resources. These embedded educational tools should render the documents more comprehensible and increase the number of resources easily available to consumers. In the end, the hope is that consumers will sit down at the closing table as more confident and informed participants.

b. The Disadvantages of eClosings

While the eClosing proposal directly addresses most of the identified problems that consumers face in mortgage closings, it does have its disadvantages.

First, the electronic format could tempt consumers to simply "click through" the documents and spend even less time reviewing documents than they did in the traditional mortgage closings. Consumers today are accustomed to quickly scrolling through electronic contracts that they encounter online and clicking the "agree" button without reviewing the contract's substantive terms.[8] If consumers adopt the same behavior in eClosings, there is a serious risk to consumer understanding.

Second, by switching to an electronic format, there is concern that the "ceremony" of the closing process will be lost. Losing a sense of "ceremony" could mean that consumers are failing to understand the importance of the financial commitments they are making through an eClosing.

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[8] Omri Ben-Shahar, The Myth of 'Opportunity to Read' in Contract Law, 5 European Review of Contract Law 1 (2009).

Third, eClosings require consumers to have access to both a computer and the Internet, yet sixteen percent of the U.S. population still does not have access to those items.[9] Furthermore, a significant portion of consumers only has access to the Internet through mobile devices, but the small screen format does not lend itself to convenient document review. Without sufficient access to the requisite technology, consumers risk not understanding the financial transaction they are completing.

3. Recommendations for CFPB's Proposal

In large part, the CFPB endorses eClosings because electronic delivery of documents provides consumers with more of an opportunity to read documents prior to closing. In fact, the "opportunity-to-read" solution features prominently in many current proposals for reform in the area of consumer contracts. Given more of an opportunity to read, so goes the line of argument, the consumer will be more informed and their assent more robust.

Recent research indicates, however, that "opportunity-to-read" solutions fail.[10] Even if given more time to read contracts, consumers will not read them. The contract language is too complicated, and the average consumer does not know how to meaningfully evaluate the content of the contract terms. Simply put, the costs of reading the contract—significant investments of time and effort—outweigh the benefits—gaining information about the deal's contingent terms.[11]

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[9] CFPB at 40.
[10] Ben-Shahar at 5-6.
[11] Id. at 7.

The Housing Initiative Clinic proposes two recommendations. First, in light of recent consumer behavior research, the CFPB should emphasize the "opportunity-to-read" aspect of eClosings less, and promote its other features, such as its ability to embed educational tools, more. Second, the CFPB should consider two alternatives to "opportunity-to-read" solutions put forward by Omri Ben-Shahar. Ben-Shahar suggests creating a rating and labeling regime for contracts. The rating regime for contracts would be akin to the Zagat rating system for restaurants. The advantage of rating contracts would be that weight is given to those aspects that the average consumer cares about the most. Those who do not want to read the mortgage closing documents can rely on a rating to guide them.[12] The labeling regime would function similarly to food nutrition labeling. The most essential contract provisions would be summarized and uniformly presented upfront for easy consumer review prior to signing the closing documents.[13]

Conclusion: Next Steps

In August 2014, the CFPB announced a plan to launch a three-month pilot program to test the feasibility of eClosings.[14] Several months later, the CFPB revealed the twelve companies it selected to participate in the pilot. The five technology vendors are Accenture Mortgage Cadence, DocMagic, Inc., eLynx, Pavaso, Inc., and PiersonPatterson, LLP. The seven lenders are Blanco National Bank, Boeing Employees Credit Union, Franklin First Financial, Ltd., Flagstar Bank, Mountain America Credit Union, Sierra Pacific Mortgage, and Universal American Mortgage

[12] Id. at 22-25.
[13] Id. at 25-26.
[14] CFPB Announces Mortgage eClosing Pilot Participants (August 21, 2014), *available at* http://www.consumerfinance.gov/newsroom/cfpb-announces-mortgage-eclosing-pilot-participants/.

Company.[15] The pilot program was supposed to wrap up in early 2015; however, no results have been released to date. If the pilot program indicates that eClosings are successfully educating and empowering consumers through streamlining the mortgage closing process, the CFPB will begin to work with industry participants to implement eClosing solutions more broadly.

[15] Ray Hagan, Prepared for Takeoff: The CFPB eClosing Pilot Program (December 4, 2014), *available at* http://nationalmortgageprofessional.com/news/51079/prepared-takeoff-cfpb-eclosing-pilot-program.